

Posner, Hayek, and the Economic Analysis of Law

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ABSTRACT: This Article examines Richard Posner's critique of F.A. Hayek's legal theory and contrasts the two thinkers' very different views of the nature of law, knowledge, and the rule of law. Posner conceives of law as a series of disparate rules and as purposive. He believes that a judge should examine an individual rule and come to a conclusion about whether the rule is the most efficient available. Hayek, on the other hand, conceives of law as a purpose-independent set of legal rules bound within a larger social order. Further, Posner, as a legal positivist, views law as an order consciously made through the efforts of judges and legislators. Hayek, however, views law as a spontaneous order that arises out of human action but not from human design. For Hayek, law as a spontaneous order—of which the best example is the common law—contains and transmits knowledge that no one person or committee could ever know and, thus, regulates society better than a person or committee could. This limits the success of judges in consciously creating legal rules because a judge is limited in the forethought necessary to connect a rule to other legal and non-legal rules and in what Hayek termed “the knowledge of particular circumstances of time and place.”

This Article also explores Posner's argument that Hayek misunderstood the “rule of law” as the “rule of good law.” Contrary to Posner, in the view Hayek came to espouse in his later work, the common law embodies the rule of law in a way that positivist creations of law do not. When judges consciously make law, it is those human actors, not the “law” as such, that “rule.” When law arises out of a spontaneous order, however, it is the law that rules. Judges merely articulate it. Posner does not distinguish between

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these two processes and, therefore, sees a difference between the rule of law and the rule of “good” law that Hayek does not. This is because for Hayek, the rule of law is meaningful only in a liberal society where law arises out of a spontaneous order.

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I. INTRODUCTION

Although Friedrich August von Hayek (1899–1992) was trained as a lawyer and earned a Nobel Prize as an economist, he has been largely ignored by modern law-and-economics scholars. Richard Posner’s recent essay comparing Hayek and Hans Kelsen through the lens of the economic analysis of law indicates why Hayek has been overlooked by the modern school of law and economics.¹ The Hayekian view of the world rests on conceptions of law, economics, and the state that are fundamentally at odds with prevailing modes of analysis. Finding this fundamental incompatibility, Posner concludes somewhat surprisingly (to both conventional wisdom as well as himself) that it is Kelsen, not Hayek, who provides a better fit with modern law-and-economics analysis.

This Article focuses on three areas of contrast between Posner’s and Hayek’s models of the economic analysis of law. This comparison, however, quickly reveals more fundamental and far-reaching distinctions between the Posnerian and Hayekian systems. At root, the two systems of law turn on radically different assumptions about the nature of knowledge and ignorance in society and the economy and about the effect that this has on the nature of the judicial process. Posner believes that judges (such as himself) are capable of collecting and applying substantial amounts of both factual and theoretical knowledge that can and should be used to inform the judicial function. Hayek, by contrast, is doubtful that *any* collective decision maker, including a judge, has the ability to collect and weigh enough information to be able to consciously develop and improve the law according to any measuring stick of social outcome.

From this fundamental disagreement about the nature of knowledge and the ability of judges to harness it, fundamental disagreements also arise about both the positive and the normative economic analysis of law. First, Posner and Hayek hold fundamentally different views about the nature of the common law, as encapsulated in Hayek’s characterization of the common law as a “spontaneous order,” in contrast to Posner’s conceptualization of the common law as essentially a collection of disparate

1. Judge Posner originally produced this essay for a conference sponsored by the European Association for Law and Economics in Vienna in 2001. See Richard A. Posner, Kelsen, Hayek, and the Economic Analysis of Law, Lecture at the Eighteenth Annual Meeting of the European Association for Law and Economics (Sept. 14, 2001) (prepared text on file with the Iowa Law Review). The essay was then included as Chapter 7 in RICHARD A. POSNER, LAW, PRAGMATISM, AND DEMOCRACY 250–91 (2003) [hereinafter POSNER, LAW, PRAGMATISM, AND DEMOCRACY]. It was again used in a symposium article in Richard A. Posner, *Hayek, Law, and Cognition*, 1 N.Y.U. J.L. & LIBERTY 147 (2005) [hereinafter Posner, *Hayek, Law, and Cognition*]. This latest version expanded upon the previous works and included some discussion of Hayek’s theory of psychology and a more general critique of Austrian economics. For the most part, this Article refers to the version in *Law, Pragmatism, & Democracy*, but it also makes use of the *New York University Journal of Law and Liberty* version.

rules. Second, these contrasting views of the common law lead to a radical difference of opinion regarding the normative purpose of law in society. Posner argues that judges should consciously use law to further designated social goals, namely wealth maximization. Hayek, by contrast, argues that the purpose of the law should be to create the conditions necessary for the maintenance of the spontaneous order of society, including the spontaneous order of the common law itself. Hayek's approach actually reinforces the traditional model of the common law as a logical system in which judges engage in analogical and doctrinal reasoning. Hayek views this as the proper role of judges, whereas Posner views it as naïve. Finally, these contrasting views of the nature of law and the role of economic analysis in law generate fundamentally different views of the rule of law. Whereas Posner contends that Hayek confuses the rule of law with the rule of *good* law or the rule of *liberal* law, the analysis presented here reveals that Hayek views the rule of law as being determined precisely by its relationship to a liberal social order and market economy. Thus, there is in fact no confusion in Hayek's use of the rule of law, but rather it may be Posner who is confused because his use of the term fails to situate it in a social context.

At bottom, Hayek argues that judges should act as common-law judges traditionally were believed to have acted: they should apply the law as it is and as it has grown over time instead of independently formulating new law untethered to the larger social order. When Posner faults Hayek for not allowing the law to evolve, he misunderstands Hayek's view of legal change. Hayek does not call for the law to remain beholden to prior custom without adapting to new circumstances. Hayek merely argues that, on the whole, *judges* should not change the law. Because law arises through a spontaneous process, it is in law's very nature that it will change. Judges should *look* to how law has changed and not *create* those changes through social planning.

The purpose of this Article is not to defend Hayek's legal theory as either an accurate descriptive model of the common law as a historical system or as a normative system on economic principles. Instead, it is primarily intended to clarify Hayek's views in order to better assess Posner's critique. As will be seen, Posner's characterization of Hayek misunderstands Hayek in some subtle, but important, ways. Hayek's model of law is rooted in the traditional common law method but justified by economic reasoning, albeit economic reasoning that differs from Posner's neoclassically grounded economics.

Part II of this Article thus begins with an explanation of the different understandings of knowledge in Hayek's and Posner's systems of economics. Part III then compares Hayek's and Posner's views of law and the judicial role in the common law. Part III addresses Posner's criticism of Hayek's understanding of the concept of the rule of law. Part IV concludes with an analysis of the accuracy and normative attractiveness of these two rival views of the economic analysis of law and provides a Hayekian response to

Posner's claim that there is no room for legal change in Hayek's legal system.

II. THE NATURE OF JUDICIAL KNOWLEDGE

The foundation for the disagreement between Posner and Hayek on the economic analysis of law is grounded in a fundamental difference between the two over the nature of knowledge and its accessibility to collective decision makers such as judges.

A. POSNER ON JUDICIAL KNOWLEDGE

The cornerstone of Posner's economic analysis of law is that judges can, do, and should use economic principles to inform their decision making and to improve the law itself. Embedded within this analysis is a fundamental assumption about the ability of judges to compile and analyze the knowledge necessary to understand the implications of their decisions and to render those that will have both the goal and effect of improving the economic efficiency of the law.

In Posner's view, when a judge announces a legal rule, he must take into consideration the future effects of that rule. For example, in a torts case, the judge should "consider the probable impact of alternative rulings on the future behavior of people engaged in activities that give rise to the kind of accident in the case before him."² In choosing between possible rules, efficiency is the paramount criterion. According to Posner, judges "might as well concentrate on increasing" efficiency because they are not well disposed, *qua* common-law judges, to enforce alternative values, such as wealth redistribution.³ Thus, Posner views judges as future-looking rule makers who decide which rules to impose on the parties before them based upon the most efficient outcome that will follow from those rules. This includes assessing what would be the most efficient outcome in circumstances where, because of transaction costs, a transaction would not occur without judicial intervention.⁴

Viewing judges as rule makers who seek the most efficient outcome begs the question of *how* judges decide what rule will be the most efficient. Posner admits as much when he states that "the economic theory of law presupposes

2. RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 26 (6th ed. 2003).

3. *Id.* at 252 n.3; *see also id.* at 533 ("If, therefore, common law courts do not have effective tools for redistributing wealth . . . it is to the benefit of all interest groups that courts . . . should concentrate on making the pie larger.").

4. *See, e.g., id.* at 250 ("[T]he common law establishes property rights, regulates their exchange, and protects them against unreasonable interference—all to the end of facilitating the operation of the free market, *and where the free market is unworkable of simulating its results.*" (emphasis added)). *See generally* Ronald H. Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960) (arguing for an approach to social arrangements that takes into account the total effect of those arrangements).

machinery for ascertaining the existence of the facts necessary to the correct application of a law."⁵ Judges must rely not only on the facts provided by the parties in the cases before them, but also on general social science data that can help judges ascertain how a legal rule will influence behavior.⁶

Posner admits that there are some limits to this view, limits that Hayek, as is discussed below, recognizes much more concretely. Posner states that in crafting new rules of law, "judges, and legal professionals in general, may be so bereft of good sources of information . . . that their most efficient method of deciding cases and resolving issues of institutional design is to follow, or at least to be strongly constrained by, precedent."⁷ Posner limits this handicap, however, to situations where social change has created conditions so removed from the judges' knowledge that precedent is the only reference point. This is not meant to imply that Posner does not believe judges should generally adhere to precedent—he does—but rather that judges should also seek outside information in crafting legal rules.

B. HAYEK ON JUDICIAL KNOWLEDGE

Hayek holds a far less optimistic view of the ability of judges to collect and synthesize the degree of knowledge necessary to engage in the far-reaching economic balancing encouraged by Posner or to even predict whether the adoption of a particular rule will make society better- or worse-off. Others have questioned whether judges are suited by training and expertise to engage in the far-ranging inquiry demanded of the Posnerian wealth-maximizing judge.⁸ Scholars have also questioned whether judges in fact are as likely to adopt wealth maximization as their primary goal, as Posner believes, instead of egalitarian or redistributive goals.⁹ Hayek's challenge, however, is more fundamental—assuming that a judge possesses the technical ability to execute the economic analysis necessary to choose the economically efficient rule and assuming further that the same judge faithfully seeks to implement his scheme, can such a judge actually predict that any decision he makes will in fact *effectuate* an improvement in the law?¹⁰ In other words, if Richard Posner himself had the time to rule on every important case, could he in fact effectuate substantial long-term improvement in the law?

5. POSNER, *supra* note 2, at 267.

6. *See id.* at 19–20; Posner, *Hayek, Law, and Cognition*, *supra* note 1, at 165.

7. *Id.* at 561.

8. *See generally* James M. Buchanan, *Good Economics—Bad Law*, 60 VA. L. REV. 483 (1974) (discussing the first edition of Posner's *Economic Analysis of Law*).

9. *See* Todd J. Zywicki, *The Rise and Fall of Efficiency in the Common Law: A Supply-Side Analysis*, 97 NW. U. L. REV. 1551, 1563–64 (2003); James E. Krier, Book Review, 122 U. PA. L. REV. 1664, 1694 (1974) (reviewing RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* (1972)).

10. 1 F.A. HAYEK, *LAW, LEGISLATION AND LIBERTY: RULES AND ORDER* 102 (1973).

The implications of the Hayekian system suggest that Hayek would say “no.” Posner recognizes this intuition: he notes that for Hayek, the notion of a “capitalist judge” would be a contradiction in terms, just as the notion of a “socialist judge” would be.¹¹ Posner indicates that he believes Hayek’s rejection of the concept of a capitalist judge rests on the normative notion of the judge’s role in society and the propriety of reading one’s personal views into the law. Posner writes, “The contradiction Hayek identifies has nothing to do with the content of the judge’s policy views. It lies rather in the judge’s allowing those views to influence his decisions.”¹² Posner concludes that, as a result, the role of a Hayekian judge is “passive,” relegated to enforcing the expectations created by custom, rather than seeking to improve the law according to socialist principles, capitalist principles, or any other principles.¹³

Although Posner is correct in observing that Hayek rejects the proper role of judges as seeking to improve the law according to capitalist or any other principles, Hayek’s rejection lies in positive, not normative, analysis. It seems evident that if judges or any other collective decision maker *could* improve the law by reading capitalist principles into it, then the judge should do so.¹⁴ The challenge, therefore, is not to determine that a judge has normative goals, but rather, to determine whether tinkering with particular legal rules on the basis of those goals will bring about the desired effect of actually improving the law.¹⁵ For Hayek, it is this step—trying to predict whether changes to the law will actually bring about the predicted and desirable economic and social effects that the judge seeks to achieve—that presents the insuperable obstacle. Thus, Hayek’s critique is not primarily grounded in the idea that it is *inappropriate* for judges to impose particular policy views in the law, but rather that it is *impossible* for judges to reliably and predictably bring about the desired policy goals that they seek to obtain.¹⁶

11. POSNER, LAW, PRAGMATISM, AND DEMOCRACY, *supra* note 1, at 277. This is drawn from Hayek’s comment in *Law, Legislation and Liberty: Rules and Order*. See HAYEK, *supra* note 10, at 121.

12. POSNER, LAW, PRAGMATISM, AND DEMOCRACY, *supra* note 1, at 277.

13. *Id.* at 278–79.

14. In this view, Hayek presumably would disagree with those, such as Buchanan, who truly do see the role of judges as being passive, implementing the policy choices made at the constitutional or political level. See Buchanan, *supra* note 8, at 490 (“[T]he judge should not change the basic law because, in such behavior, he would be explicitly abandoning his role of jurist for that of legislator.”).

15. *But see* Eric Mack, *Hayek on Justice and the Order of Actions*, in THE CAMBRIDGE COMPANION TO HAYEK 259, 281–82 (Edward Feser ed., 2006) (arguing that Hayek might contend that not only is there the problem of knowing the facts necessary to design legal rules, but also in designing legal rules, one must create a hierarchy of ends that different individuals will not be able to agree upon).

16. HAYEK, *supra* note 10, at 102 (noting that the judge “will never be able to foresee all the consequences of the rule he lays down”); *cf.* G. Marcus Cole, *Shopping for Law in a Coasean*

Hayek's view as to the proper role of the judge derives from his observations regarding the ability of judges to overcome their ineradicable knowledge of the effects of their decisions and, hence, their inability to predict whether their decisions will actually advance or retard the achievement of their desired goals.¹⁷ In turn, this suggests that although Posner is correct in noting that Hayek sees the role of the judge as limited to enforcing parties' legitimate expectations, this does *not* mean that judges are "passive." Rather, they still retain the task of distinguishing legitimate from illegitimate expectations, determining how particular rules fit within the larger overall framework of rules, and determining how legal and non-legal rules have changed.¹⁸

Judges, Hayek argues, are fundamentally ignorant about almost all of the effects and consequences of their decisions.¹⁹ The inability of judges to foresee the full implications of their decisions arises from the inherent complexity of society and the fundamental inability of judges to collect all of the information that would be necessary to determine whether, in fact, any given rule will tend to increase economic wealth in the long run.²⁰ As Hayek states, "Law-making is necessarily a continuous process in which every step produces hitherto unforeseen consequences for what we can or must do next."²¹ To understand fully why judges cannot predict the full consequences of their decisions, it is necessary to review Hayek's understanding of knowledge and how that pertains to judicial decision making.

In his famous essay, *The Use of Knowledge in Society*, Hayek addresses the issue of the nature of knowledge in the context of central economic planning under socialism.²² As will become apparent, however, the challenge of economic planning under socialism is readily applicable to the challenge of a wealth-maximizing Posnerian judge.²³ As Hayek notes, the "economic problem of society is thus not merely a problem of how to allocate 'given' resources It is rather a problem of how to secure the best use of resources known to any of the members of society, for ends whose relative importance only those individuals know."²⁴ This decision, in

Market, 1 N.Y.U. J.L. & LIBERTY 111, 115 (2005) ("[V]ery complex orders, comprising more information than any one brain could possibly access, can only be brought about spontaneously.").

17. See HAYEK, *supra* note 10, at 102, 117.

18. These attributes of Hayek's system are discussed in greater detail *infra* Parts IV–V.

19. See HAYEK, *supra* note 10, at 65.

20. See *id.*

21. *Id.*

22. F.A. Hayek, *The Use of Knowledge in Society*, 35 AM. ECON. REV. 519 (1945), reprinted in THE ESSENCE OF HAYEK 211, 213 (Chiaki Nishiyama & Kurt Leube eds., 1984).

23. See generally Gerald P. O'Driscoll, Jr., *Justice, Efficiency, and the Economic Analysis of Law: A Comment on Fried*, 9 J. LEGAL STUD. 355 (1980).

24. Hayek, *supra* note 22, at 212.

turn, necessitates a second decision—should we place primary authority for economic decisions in particular contexts in the hands of private economic actors or in the hands of centralized decision makers such as central planners or judges? Answering this question leads to a corollary—should social institutions, such as law, be designed primarily to try to efficiently funnel dispersed knowledge from individuals to centralized decision makers, or should social institutions primarily seek to convey to decentralized private economic decision makers such additional knowledge as they need in order to enable them to dovetail their plans with those of others?²⁵ Posner suggests that the purpose of social institutions should be to accomplish the former—to funnel information about individual preferences, constraints, and the like to judges, who can then weigh these various elements and come out with a rational resource allocation.²⁶ Hayek indicates by contrast that the purpose of law is to provide to dispersed economic decision makers the “additional knowledge” necessary to rationally plan their own affairs.²⁷ Hayek states the puzzle:

This is not a dispute about whether planning is to be done or not. It is a dispute as to whether planning is to be done centrally, by one authority for the whole economic system, or is to be divided among many individuals. . . . Competition . . . means decentralized planning by many separate persons.²⁸

In other words, the question is whether the purpose of the law is to accomplish some overall social objective or plan, such as suggested by Posner, or whether the law is designed to serve as an input to individual expectations in order to enable individuals to effectuate their *own individual* plans by coordinating their affairs with others who are necessary to effectuating those plans.

An example of Hayekian versus Posnerian planning might be the development of products-liability law. Traditionally, products-liability law was hedged with concepts of negligence, contributory negligence, and contract law.²⁹ These were doctrines that had evolved over centuries and were recognized by judges as the established rules of relations between manufacturers, distributors, and consumers. Then, largely on account of judges following the innovations of law-and-economics research, judges

25. *Id.* at 213.

26. *See* Posner, *Hayek, Law, and Cognition*, *supra* note 1, at 164–65.

27. *Id.*

28. *Id.*; *see also* Todd J. Zywicki, *Epstein and Polanyi on Simple Rules, Complex Systems, and Decentralization*, 9 CONST. POL. ECON. 143, 147 (1998) (explaining the difference between simple and complex rules).

29. *See generally* RICHARD A. EPSTEIN, *MODERN PRODUCTS LIABILITY LAW* (1980) (discussing the history of products-liability law).

deliberately developed strict products-liability rules.³⁰ This was heralded as a great achievement because it imposed new legal rules derived from economic efficiency calculations rather than evolved doctrine.³¹ However, there is good reason to conclude that strict liability has proven less efficient in the long run than the evolved regime it replaced and that the unanticipated consequences and individual responses have illustrated the perils of judicial central planning, rather than its promise. For instance, it may have encouraged moral hazard by allowing for the misuse of products, while still allowing misusing consumers to sue. Further, it has ignored the ways in which tort law was just one compensation-and-deterrence system among several, such as insurance, name brands and trademarks, and third-party quality assessments (such as *Consumer Reports* magazine or Underwriters Laboratories). So, arguably at least, by imposing a blanket mandatory rule rather than the old rule that had evolved, and by failing to anticipate the full range of individual responses, strict products liability takes the law in the wrong direction.

Whether strict products liability actually is more or less efficient than the regime it supplanted is not the point. Rather, the point is that it *could be* less efficient despite the best efforts of highly educated and capable judges. The difficulty is not the education of judges, but the inability to predict every possible response. Products liability is merely an example of where judges venture forth to provide a new legal rule when they may not—and according to Hayek *cannot*—have enough knowledge to justify that they do so.³²

To further understand whether the purpose of law should be to funnel information from market actors to judges or from judges to market actors (as with strict products-liability law), it is necessary to understand the nature of knowledge in the Hayekian system. Hayek distinguishes between two types of knowledge—scientific knowledge and “knowledge of the particular circumstances of time and place.”³³ The latter form of knowledge, Hayek emphasizes, is the essence of economic knowledge.³⁴ It consists of such acts as knowing of and putting to use a machine not fully employed, reallocating a particular individual to a position where his skills can be better used, or being aware of a surplus stock of goods that can be drawn upon during an

30. See Mark A. Geistfeld, *Products Liability*, in 3 ENCYCLOPEDIA OF LAW AND ECONOMICS 347, 348 (Boudewijn Bouckaert & Gerrit De Geest eds., 2000), available at <http://encyclo.findlaw.com/5140book.pdf> (“Today efficiency considerations often strongly influence the formulation of products liability laws . . .”); see also GUIDO CALABRESI, *THE COST OF ACCIDENTS* 166 (1970) (describing how manufacturers will be responsible for insuring against liability resulting from accidents involving their products).

31. See Geistfeld, *supra* note 30, at 348.

32. HAYEK, *supra* note 10, at 12.

33. Hayek, *supra* note 22, at 214.

34. See *id.* at 214.

interruption of supplies.³⁵ This type of knowledge is simply not the type of knowledge that can be easily transmitted to a centralized decision maker, and in some cases it cannot be transmitted at all.³⁶ It includes tacit knowledge and other similar types of knowledge but not express costs-and-benefits data. For decision makers seeking to make maximum use of this knowledge of time and place, it is necessary that they have “additional knowledge.”³⁷

C. HAYEK AND POSNER ON “PRICES” AND “PLANNING”

1. Prices, Information, and Equilibrium

Hayek focuses on the price system as an institution that provides the type of “additional knowledge” that individuals need in order to make efficient use of decentralized knowledge.³⁸ He uses the example of a change in the market for tin, such as an increase in demand through a new use for tin or a decrease in supply through the elimination of a source of tin.³⁹ It does not matter whether there is an increase in demand or a decrease in supply—in fact, as Hayek stresses, it is significant that it does not matter what caused the tin scarcity.⁴⁰ “All that the users of tin need to know,” he observes, “is that some of the tin they used to consume is now more profitably employed elsewhere and that, in consequence, they must economize tin.”⁴¹ Most users of tin need not know where the more urgent need has arisen or why.⁴² Only a small number of users need to know of the initial scarcity for information to be transmitted through the price system to signal that tin has become scarcer.⁴³ Hayek illustrates the chain of information transmission that conveys to end users of tin the need to conserve or make more efficient use of tin:

If only some [users of tin] know directly of the new demand, and switch resources over to it, and if the people who are aware of the new gap thus created in turn fill it from still other sources, the effect will rapidly spread throughout the whole economic system and influence not only all the uses of tin but also those of its substitutes and the substitutes of these substitutes, the supply of all the things made of tin, and their substitutes, and so on; and all of

35. *Id.*

36. *Id.* at 217.

37. *Id.* at 213.

38. Hayek, *supra* note 22, at 219. Or, indeed, to make investments to develop this sort of tacit and decentralized knowledge. *See id.*

39. *Id.* at 218.

40. *Id.* at 219.

41. *Id.*

42. *Id.*

43. Hayek, *supra* note 22, at 219.

this without the great majority of those instrumental in bringing about these substitutions knowing anything at all about the original cause of these changes. The whole acts as one market, not because any of its members survey the whole field, but because their limited individual fields of vision sufficiently overlap so that through many intermediaries the relevant information is communicated to all.⁴⁴

Posner, by contrast, uses an example of milk delivery in New York City, which at first glance appears to illustrate the same point as Hayek's tin mine. "No milk czar decides how much milk is needed when and by whom and then obtains the necessary inputs, which include dairy farms and farmers, milk-supply plants, refrigerated milk trucks, packaging equipment and materials, accounting and other support activities, and the scheduling and provision of delivery to retail outlets."⁴⁵ The only coordinator that brings together all these suppliers of raw materials, labor, and capital is the price system.⁴⁶ Moreover, not only are they coordinated *within* the milk distribution system, the milk distribution system is coordinated with still *other* markets, regionally, nationally, and even globally.⁴⁷

But by altering Hayek's example, it appears that Posner has in fact also inadvertently, but importantly, recharacterized Hayek's point. Hayek chose this example to illustrate the *dynamic* nature of markets and the price system, which responds in a rapid and decentralized manner to an exogenous demand or supply shock.⁴⁸ Posner's example, by contrast, is one of a *static* analysis of the market and the coordination of the many individuals in the market. While the market, of course, performs both functions, the choice of examples also illustrates a subtle difference of mindset in the different ways that Hayek and Posner view the law and other social institutions, such as markets. For Posner, the world is essentially orderly, predictable, and in equilibrium.⁴⁹ The fundamental social problem, therefore, is how to arrange social, legal, and economic institutions so as to maximize social wealth in equilibrium. Coordination of individual activity is essentially taken for granted, and the goal is to ensure that this coordination occurs at the level of interaction that maximizes social wealth.

For Hayek, by contrast, the world is fundamentally in disequilibrium, although constantly trying to move toward equilibrium.⁵⁰ The marvel is not that coordination occurs without the oversight of a "milk czar," but rather that coordination occurs *at all* in light of the fact that coordination *could not*

44. *Id.*

45. Posner, *Hayek, Law, and Cognition*, *supra* note 1, at 149.

46. *Id.*

47. *Id.*

48. *See* HAYEK, *supra* note 10, at 104.

49. *See* Posner, *Hayek, Law, and Cognition*, *supra* note 1, at 162-63.

50. *See* HAYEK, *supra* note 10, at 105.

be imposed by any milk czar. Every action by any individual creates a new perturbation to the system—a new use for tin or the elimination of a source of tin. From a civil war in Zambia to a flat tire in Brooklyn, there are constant disruptions to the flow of goods and services. The miracle, therefore, is that coordination can emerge from this chaotic stew of disparate individual actions and motivations. For Hayek, therefore, the goal of social institutions—including law—is fundamentally to enable smooth individual *coordination*.⁵¹ Coordination cannot be taken for granted—smooth coordination results only from the existence of social institutions that enable individuals to predict one another's actions.⁵²

Indeed, Hayek's understanding of equilibrium itself differs from the standard neoclassical model that underlies Posner's example.⁵³ The differences between the two conceptions of equilibrium are worth elaborating upon here, as they relate directly to Hayek's and Posner's views on the ordering power of the common law. The standard understanding of equilibrium describes a collective-market phenomenon, where supply and demand are in balance.⁵⁴ "General equilibrium" is thus a model of an entire economy where all markets "clear."⁵⁵ All that is necessary for a market to be in equilibrium, therefore, is to assume that all relevant parties have full knowledge of prevailing market prices so that they know the relevant price at which to transact.⁵⁶ For Hayek, however, equilibrium does not describe "a market," rather it describes an *individual* phenomenon, specifically, the coordination of the various plans formulated and pursued by individual economic actors.⁵⁷ Equilibrium is thus a matter of *individual* coordination of plans rather than a description of a *social* pattern.⁵⁸ In a society based on exchange, once equilibrium is conceived of as coordination of individual plans, it becomes evident that the most important information is *not* the price of various goods, but rather the predictability of the actions of other people with whom one wants to trade. As Hayek puts it:

since some of the "data" on which any one person will base his plans will be the expectation that other people will act in a particular way, it is essential for the compatibility of the different

51. *See id.* at 106–07.

52. *Id.*

53. *See* F.A. Hayek, *Economics and Knowledge*, in 4 *ECONOMICA* 33 (1937), *reprinted in* L.S.E. *ESSAYS ON COST* 45 (James M. Buchanan & George F. Thirlby eds., 1981).

54. *See* POSNER, *supra* note 2, at 8.

55. *See id.*

56. *See id.*

57. Hayek, *supra* note 53, at 48–49.

58. *Id.* at 49–50.

plans that the plans of the one contain exactly those actions which form the data for the plans of the other.⁵⁹

To say that “society” is in a state of equilibrium, therefore, “means only that compatibility exists between the different plans which the individuals composing it have made for action in time.”⁶⁰ He adds:

It appears that the concept of equilibrium merely means that the foresight of the different members of the society is in a special sense correct. It must be correct in the sense that every person’s plan is based on the expectation of just those actions of other people which those other people intend to perform, and that all these plans are based on the expectation of the same set of external facts, so that under certain conditions nobody will have any reason to change his plans. . . . [Correct foresight] is . . . the defining characteristic of a state of equilibrium.⁶¹

Equilibrium is thus disturbed whenever one person changes his plans, thereby upsetting the interwoven plans of others. A plan may change either as the result of an internal impulse (simply a subjective change of mind) or in response to an external stimulus (such as an unexpected collapse of a tin mine). As illustrated in his example of the New York milk market, Posner sees the key economic question as one of the coordination of the division of labor through the price system, thereby enabling milk to be delivered efficiently to the proper location.⁶² Hayek, however, stresses that in addition to the division of labor, there is also a problem of the division of *knowledge*.⁶³ This describes not just the problem of the efficient distribution of milk, but also the more complicated question of how parties decide whether to manufacture, distribute, and consume milk instead of yogurt, ice cream, cheese, or dairy products at all.⁶⁴ The value of the price system, therefore, is to send signals to market actors as to how much dairy product to produce, what kinds of dairy products to produce, and, even more far-reaching, whether to allocate a given parcel of land to dairy farming at all or to something else.⁶⁵ By focusing only on the coordination of the division of

59. *Id.* at 50–51.

60. *Id.* at 53.

61. *Id.* at 54.

62. See Posner, *Hayek, Law, and Cognition*, *supra* note 1, at 149 (“There is no coordination—except price.”).

63. Hayek, *supra* note 53, at 63–64.

64. See *id.* at 63 (stating that how different commodities are used is the larger aspect of the problem of knowledge).

65. Hayek states:

[P]rice expectations and even the knowledge of current prices are only a very small section of the problem of knowledge as I see it. The wider aspect of the problem of knowledge with which I am concerned is the knowledge of the basic fact of how the different commodities can be obtained and used, and under what

labor, Posner essentially ignores this larger context and the larger value of the information transmitted by the price system. The price system allows individual consumer decisions about preferences for milk to be transmitted through many steps to decisions about how many cows a dairy farmer should own and even whether his farm is better used as a dairy farm or a strip mall in light of future expectations of competing needs. Prices thus enable parties to better coordinate their plans by enabling them to predict how other parties are likely to act in the future.

2. Who Plans?

To understand whether the purpose of law should be to funnel information from market actors to judges or, instead, from judges to market actors, it is first necessary to understand the nature of knowledge in the Hayekian system.

Hayek distinguishes between two types of knowledge—scientific knowledge and “knowledge of the particular circumstances of time and place.”⁶⁶ Hayek never expressly defines the concept of scientific knowledge except in contrast to its alternative. In general, scientific knowledge seems to refer to knowledge of general and scientifically falsifiable rules. In the context of economics, Hayek implicitly uses the term to refer to economic decision making by a panel of experts who can acquire and synthesize all relevant economic information and allocate resources rationally according to some specified general rule, such as to ensure that economic resources are allocated such that the marginal rate of substitution of all economic goods is equal across the economy. As Hayek states, “If we possess all the relevant information, *if* we can start out from a given system of preferences, and *if* we command complete knowledge of available means, the problem which remains is purely one of logic.”⁶⁷ At that point, it would be “just” a problem of working out many billions of mathematical equations to allocate resources according to the general rule.⁶⁸ If all of these criteria were somehow met, then the economy would become one massive, but logically solvable, technical problem that experts could theoretically resolve according to some plan.

On the other hand, again, the essence of economic knowledge is the “knowledge of the particular circumstances of time and place.”⁶⁹ This

conditions they are actually obtained and used . . . that is, the general question of why the subjective data to the different persons correspond to the objective facts.

Id.

66. *Id.* at 214–15.

67. *Id.* at 211.

68. As Hayek notes, however, even if this were possible, it still leaves open the question of how the experts themselves should be chosen, a question that cannot be resolved on purely scientific grounds. Hayek, *supra* note 53, at 213.

69. *Id.* at 214.

consists of the “facts on the ground” that individuals in the economy must gather and assess in making their own local economic decisions. As such, it cannot be easily communicated to a centralized decision maker and often, due to its particularized and perhaps infinite nature, cannot be transmitted at all.⁷⁰ It includes unspoken tacit knowledge but not express costs and benefits data.⁷¹ Planners who hope to use this knowledge of time and place require “additional knowledge.”⁷²

3. Legal Rules and “Planning”

For Hayek, legal rules are another social institution similar to that of prices. Legal rules convey information to individual actors about how they should behave and permit accurate predictions about how *other* people are likely to behave, thereby enabling a more seamless dovetailing of expectations and individual plans.⁷³ “[T]he system of rules into which the rules guiding the action of any one person must be fitted does not merely comprise all the rules governing his actions but also the rules which govern the actions of the *other members of the society*.”⁷⁴ This emphasis on coordination is illustrated in Hayek’s subtle observation, for instance, that property law operates “not by directly assigning particular things to particular persons, but by making it possible to derive from ascertainable facts to whom particular things belong.”⁷⁵ This knowledge, in turn, specifies who has the authority to decide to what use, among many competing possible uses, particular things can be put. But even more importantly, it enables *others* to unambiguously recognize who has authority to use or dispose of those resources.

Prices and legal rules, however, are not the exclusive social institutions that perform these sorts of functions. Tradition is a particularly powerful and important source of rules that provides guidance as to parties’ legitimate expectations of one another’s actions and, therefore, improves interpersonal coordination.⁷⁶ Greater coordination among people governed by a set of social, legal, and economic rules enables each individual to make maximum use of his local knowledge and to accomplish his own goals.⁷⁷ In

70. *Id.* at 217.

71. *See id.*

72. *See id.* at 213.

73. Thus, both legal rules and economic prices comprise some of the “external facts” that parties rely upon in coordinating their plans with one another. *See* text accompanying *supra* note 61. As Marcus Cole observes, Hayek’s analogy between prices and legal rules is imperfect. *See* Cole, *supra* note 16, at 121–22. The difficulties in the analogy identified by Professor Cole do not appear to undermine the use of the analogy as discussed here.

74. F.A. HAYEK, LAW, LEGISLATION, AND LIBERTY: THE MIRAGE OF SOCIAL JUSTICE 25 (1976) (emphasis added).

75. *Id.* at 37.

76. *See* HAYEK, *supra* note 10, at 85–88.

77. *See id.* at 99.

turn, enabling individuals to maximize the use of their local knowledge is the necessary condition for prosperity and wealth maximization.⁷⁸

This observation about the importance of tradition as a provider of social rules to further the goal of interpersonal coordination has an additional implication for understanding the role of judges in Hayek's system versus Posner's. A characteristic feature of Posner's jurisprudence is an implicit belief in legal-centrism, which is the idea that law is the primary and often determinate system of rules for determining social outcomes. Thus, whether the field under study is divorce, bankruptcy, torts, or employment discrimination, Posner implicitly assumes that the actions of the parties subject to those legal rules are determined primarily by those rules and the incentives they create.⁷⁹ Hayek, by contrast, recognizes that legal rules are merely one of many different sets of social rules that govern interactions.⁸⁰ This recognition further complicates the efforts of a judge seeking to determine the "efficient" rule in any given situation. A Posnerian judge will thus face a three-fold challenge. First, the judge must possess sufficient learning, information, and expertise to be able to determine the efficient legal rule in isolation. Second, the judge must be able to determine whether the efficient rule in isolation is also the efficient rule when embedded in and interacting with *other* relevant legal rules. But finally, the judge must be able to discern how the legal rule interacts with other *non-legal* rules that may be relevant to the determination.⁸¹

Consider, for instance, the concept of fiduciary duty in Anglo American corporate law. Imagine a judge attempting to determine whether to impose a scheme of fiduciary duty on corporate officers and directors, as opposed to a contractarian approach. First, the judge would need to know whether governance by fiduciary duty is an efficient rule, a debate that goes back generations and has attracted the attention of many of the leading and most economically sophisticated judges and legal thinkers. Second, the determination of the existence and efficient scope of fiduciary duty in any given situation also will depend on the rules of contract that prevail and, in particular, on how courts treat relational contracts as opposed to discrete contracts. Other areas of law may also be relevant. Finally, the efficacy of fiduciary duty as a restraint on managerial agency costs may also be a function of more diffuse social norms and traditions. For instance, there appear to be substantial differences among countries and cultures in the

78. *See id.*

79. Posner, *Hayek, Law, and Cognition*, *supra* note 1, at 151.

80. *See* HAYEK, *supra* note 10, at 74.

81. *See id.* at 26 ("This may well mean that the rule one ought to follow in a given society and in particular circumstances in order to produce the best consequences, may not be the best rule in another society where the system of generally adopted rules is different.").

levels of interpersonal and social trust.⁸² It is plausible that the level of social trust would be an important consideration in determining whether a given society can be best governed by broad and informally defined concepts such as fiduciary duty, rather than by more specific contractarian, regulatory, and rule-bound concepts.⁸³

Stated more concretely, while high-trust societies such as the United States can govern large corporations by fiduciary duty, in a low-trust society such as Russia, reliance on fiduciary duty may be an invitation to looting and self-dealing by corporate directors. In turn, the difficulty of structuring low-cost, effective substitutes for fiduciary duty obligations in low-trust societies has the effect of limiting the size and scale of corporations in low-trust societies. Francis Fukuyama argues, for instance, that in order to minimize the agency problems associated with a separation of ownership and control, corporations in low-trust societies tend to be family-owned and to operate on a relatively small scale, as opposed to the far-flung separation of ownership and control in American corporations, characterized by widely held stock holdings.⁸⁴ In turn, a society dominated by family-owned corporations will generate its own set of financial, market, and legal institutions that will differ dramatically from other societies. Imposing the “wrong” legal rule, therefore, will have the additional consequence of causing private actors to try to develop new self-help systems and other market responses to compensate for the unfortunate rule.⁸⁵

This example, as well as the earlier example of strict products-liability law,⁸⁶ reveals the profound difficulties involved in determining an efficient rule in isolation, much less understanding it with reference to other substantive bodies of law (such as contract law) and larger market and social institutions (such as levels of trust). Hayek would likely argue it is hubristic

82. See Paul J. Zak & Stephen Knack, *Trust & Growth*, 111 *ECON. J.* 295, 296 (2001) (presenting a study that determines why trust varies across societies).

83. For an argument along these lines, see Lynn A. Stout, *On the Export of U.S.-Style Corporate Fiduciary Duties to Other Cultures: Can a Transplant Take?*, in *GLOBAL MARKETS, DOMESTIC INSTITUTIONS: CORPORATE LAW AND GOVERNANCE IN A NEW ERA OF CROSS-BORDER DEALS* 46 (Curtis J. Milhaupt ed., 2003).

84. FRANCIS FUKUYAMA, *TRUST: THE SOCIAL VIRTUES AND THE CREATION OF PROSPERITY* 49–50 (1995).

85. An example is the American experience with the Robinson–Patman Act, an antitrust statute that, among other things, prohibits “price rebates” to consumers. 15 U.S.C. § 13(a) (2000). Subsequent interpretations of Robinson–Patman have held that coupons are not price rebates and, thus, do not run afoul of the Robinson–Patman Act. See *Fed. Trade Comm’n v. Fred Meyer, Inc.*, 390 U.S. 341, 358 (1968). As a result, even though the Act clearly is inconsistent with competition and consumer welfare, the ability to easily circumvent it through the issuance of coupons substantially ameliorates the harm caused by the Act. In turn, American consumers have developed an expectation of using coupons in shopping, and advertisers have developed marketing schemes around them. This is provided as evidence of the manner in which legal rules interact with market practices in unpredictable ways.

86. See *supra* notes 29–32 and accompanying text.

for a judge confronted with such challenges to try to rewrite the law according to any defined criteria, whether they seek to support efficiency, social justice, or feminist notions of equality. Instead, given that there are radical limits on the judge's ability to predict the full effects of his decision, the wise judge would also be a modest judge and would thus attempt to establish the parties' legitimate expectations with respect to the interaction in question. This would minimize the disruptive effect of legal rules and help to preserve interpersonal coordination.

III. PURPOSES OF LAW

The purpose of law for Hayek, therefore, is to preserve legitimate expectations and to enable interpersonal coordination and not to try to accomplish some end-state goal. Law provides order and predictability in a world characterized by unpredictability and "flux."⁸⁷ This also explains why, contrary to Posner's statements, Hayek does not consider the judicial role to be "passive."⁸⁸ Posner mistakes modesty for passivity. A Hayekian judge merely has a different responsibility from a Posnerian judge. Whereas Posner exhorts judges to decide cases so as to further some external standard of value, such as wealth maximization, a Hayekian judge has the more modest responsibility of ensuring the internal consistency of his own decision within the overall operation of the spontaneous order—or, perhaps more accurately, spontaneous *orders*—in which the judge acts.

Hayek justifies this emphasis on "immanent criticism"—or the internal consistency of particular rules within an overarching system of rules—by arguing that this approach to law is most likely to maximize interpersonal coordination.⁸⁹ Because the purpose of law is to provide guidance to individual actors as to the predicted behavior of other individuals, law serves to preserve legitimate expectations.⁹⁰ It follows, Hayek argues, that legitimate expectations are best preserved by making legal rules internally consistent within a given set of rules.⁹¹ When confronted with a dispute that cannot be resolved by settled rules, Hayek argues that the judge's task is to make any new rule cohere smoothly within the set of existing rules.⁹² "If the decision cannot be logically deduced from recognized rules, it still must be consistent with the existing body of such rules in the sense that it serves the same order of actions as these rules."⁹³ Therefore, judges should not engage

87. Mario Rizzo, *Law Amid Flux: The Economics of Negligence and Strict Liability in Tort*, 9 J. LEGAL STUD. 291, 291 (1980) (discussing the economic-efficiency approach to the analysis of the common law).

88. POSNER, LAW, PRAGMATISM, AND DEMOCRACY, *supra* note 1, at 277.

89. HAYEK, *supra* note 10, at 118–19.

90. *Id.* at 119.

91. *Id.* at 115.

92. *Id.* at 116.

93. *Id.* at 115–16.

in an external critique of the “efficiency” of legal rules but, instead, should engage in a process of internal or “immanent criticism” of the extent to which any given legal rule or decision coheres with other related and conceptually surrounding rules.⁹⁴ “[A]dvance here is achieved,” Hayek writes, “by our moving within an existing system of thought and endeavouring by a process of piecemeal tinkering, or ‘immanent criticism’, to make the whole more consistent both internally as well as with the facts to which the rules are applied.”⁹⁵ Indeed, Hayek marks this emphasis on “immanent” versus external criticism as a distinguishing feature of “evolutionary (or critical)” rationalism as opposed to “constructivist (or naïve) rationalism.”⁹⁶ Hayek argues that by focusing on improving the internal coherence of the legal system rather than on improving the legal system relative to some external benchmark, the judge thereby upholds the parties’ legitimate expectations and acts as “a servant endeavouring to maintain and improve the functioning of the existing order.”⁹⁷ By nurturing the operation of the legal order through improvement of its internal coherence, the judge helps to maintain the overall coordination of society and of the economy that depends on legal order.⁹⁸

The Hayekian judge, thus, is not passive simply because he rejects the notion that a judge can or should try to remake society according to some more egalitarian or efficient standard of value.⁹⁹ Rather, the judge should strive to preserve parties’ legitimate expectations. Note, however, that preservation of legitimate expectations often will be best furthered not by rote adherence to precedent, but by a prudent and thoughtful updating of rules to adapt to changing needs and expectations.¹⁰⁰ In particular, because legal rules are just one element of the set of rules and practices that guide individual behavior in society, changes in non-legal rules may also affect legal rules such that in order to best preserve expectations and predictability about others’ actions, it will become necessary to amend some legal rules to better cohere with changing legal and non-legal rules.¹⁰¹ The objective is to increase social coordination such that individuals will have maximum freedom to act on local information as it arises. Interpersonal coordination, not aggregate economic efficiency, should be the overarching goal of the legal system. Hayek writes:

94. HAYEK, *supra* note 10, at 118.

95. *Id.*

96. *Id.*

97. *Id.* at 119.

98. *Id.*

99. As Hayek states the matter, “There is little significance in being able to show that if everybody adopted some proposed new rule a better overall result would follow, so long as it is not in one’s power to bring this about.” HAYEK, *supra* note 10, at 119.

100. *Id.* at 116.

101. The nature of legal change in Hayek’s view is further examined *infra* Part V.

The distinctive attitude of the judge thus arises from the circumstance that he is not concerned with what any authority wants done in a particular instance, but with what private persons have “legitimate” reasons to expect, where “legitimate” refers to the kind of expectations on which generally his actions in that society have been based. The aim of the rules must be to facilitate that matching or tallying of the expectations on which generally his actions in that society have been based. The aim of the rules must be to facilitate that matching or tallying of the expectations on which the plans of the individuals depend for their success.¹⁰²

It is thus tempting to treat Hayek as a purely formalistic adherer to precedent, but such a view does not appear to be accurate. Such an interpretation of Hayek misunderstands two elements of his thought. First, Hayek’s view of precedent differs from the prevailing modern view of precedent—one that is accepted by Posner. Second, Hayek differs from Posner regarding the relevant unit of analysis for the study and evolution of legal rules. Whereas Posner examines law at the level of the *individual* rule, Hayek views the relevant level of analysis to be the *system* of rules. In other words, where Posner sees individual selection as the unit of selection for legal analysis and change, Hayek sees group selection among groups of rules as the operative model. Both points require some elaboration.

A. PRECEDENT

Hayek’s view of precedent differs from the prevailing modern view of precedent. Modern scholars operating under the mindset of legal positivism view the utility of precedent as serving to create and maintain expectations of parties about particular legal rules.¹⁰³ For most of the history of the common law, although judges followed precedent where available, they did not follow the doctrine of *stare decisis*.¹⁰⁴ Most commentators today collapse the two, treating precedent and *stare decisis* interchangeably.¹⁰⁵ The key distinction is that under a principle of *stare decisis*, a single case authored by an authoritative court standing alone is binding in all subsequent cases; whereas precedent, as traditionally applied, arose only through a pattern of several cases decided in agreement with one another, thereby giving rise to a presumption of the correctness of the legal principle. Plucknett observes,

102. HAYEK, *supra* note 10, at 98.

103. See GERALD J. POSTEMA, BENTHAM AND THE COMMON LAW TRADITION 211–13 (1986) (noting the positivist roots of *stare decisis*); Harold J. Berman & Charles J. Reid, Jr., *The Transformation of English Legal Science: From Hale to Blackstone*, 45 EMORY L.J. 437, 514 (1996) (characterizing the strict doctrine of precedent as “essentially a positivist theory, more congenial to the codification movement but grafted onto the doctrine of precedent”).

104. See Zywicki, *supra* note 9, at 1565–81 (discussing the historical use of precedent and *stare decisis*).

105. See *id.* at 1566 (collecting sources).

“An important point to remember is that one case constitutes a precedent; several cases serve as evidence of a custom It is the custom which governs the decision, not the case or cases cited as proof of the custom.”¹⁰⁶ He adds, “A single case was not a binding authority, but a well-established custom (provided by a more or less casual citing of cases) was undoubtedly regarded as strongly persuasive.”¹⁰⁷

Traditionally, therefore, judicial decisions in particular cases were thought to *illustrate* or “discover” principles of law but were not themselves the *source* of authoritative law.¹⁰⁸ Hayek approvingly quotes Lord Mansfield’s aphorism that “the common law ‘does not consist of particular cases, but of general principles, which are illustrated and explained by those cases.’”¹⁰⁹ Lord Holt, for instance, observed, “The law consists not in particular instances and precedents, but in the reason of the law”¹¹⁰ Coke, who due to his extensive collection of cases had the resources to review precedent much more than previous judges, even so described precedent as “examples” of the “true rule” and not “in and of themselves authoritative sources of those rules.”¹¹¹ As a result, the traditional common law judge was not “bound by any past articulation of that law, never absolutely bound to follow a previous decision, and always free to test it against his tradition-shaped judgment of its reasonableness.”¹¹²

For most of the common law’s history, therefore, the force of precedent derived from its persuasiveness and “congruence of legal decisions with expectations, reason, and judgment,” not from its binding force as authoritative *stare decisis*.¹¹³ The value of the rule or principle was demonstrated by the independent endorsement of several judges examining the wisdom of the rule rather than the authority of its author.¹¹⁴ Precedent was understood as a tradition derived from the decisions of a multitude of independent judges acting over the years and not the sovereign work of a “law-making” judge. The stricter form of *stare decisis*—that a decision in one

106. THEODORE F.T. PLUCKNETT, *A CONCISE HISTORY OF THE COMMON LAW* 347 (5th ed. 1956).

107. *Id.*; see also A.K.R. KIRALFY, *POTTER’S HISTORICAL INTRODUCTION TO ENGLISH LAW AND ITS INSTITUTIONS* 275–77 (4th ed. 1958).

108. Zywicki, *supra* note 9, at 1568–69; see also Berman & Reid, *supra* note 103, at 445.

109. HAYEK, *supra* note 10, at 86 (quoting W.S. HOLDSWORTH, *SOME LESSONS FROM LEGAL HISTORY* 18 (1928) (quoting Mansfield)).

110. C.H.S. FIFOOT, *LORD MANSFIELD* 16 (1936) (quoting Holt).

111. Berman & Reid, *supra* note 103, at 447; see also CARLETON KEMP ALLEN, *LAW IN THE MAKING* 143–50 (2d ed. 1930).

112. POSTEMA, *supra* note 103, at 194–95.

113. Zywicki, *supra* note 9, at 1578.

114. See J.G.A. POCKOCK, *Burke and the Ancient Constitution: A Problem in the History of Ideas*, in *POLITICS, LANGUAGE & TIME: ESSAYS ON POLITICAL THOUGHT AND HISTORY* 202, 213 (1971); A.C. Pritchard & Todd J. Zywicki, *Finding the Constitution: An Economic Analysis of Tradition’s Role in Constitutional Interpretation*, 77 N.C. L. REV. 409, 491 (1999).

case binds subsequent decisions—did not emerge until the mid-nineteenth century, reflecting the rise of legal positivism and the accompanying belief that law is created by a particular judge's decision rather than discovered as a principle from the decentralized and spontaneous agreement of several independent judges over time.¹¹⁵

Hayek, therefore, calls for judges simply to follow the example of traditional common law judging and enforce the settled principles embedded in the law.¹¹⁶ This is in opposition to the view of judges “making” law and binding, through *stare decisis*, future judges to their enlightened commands. Thus, following the traditional common law vision of precedent, Hayek believes that it is the legal *principle* that should be followed, not the precise terms of the rule itself.¹¹⁷ Although compliance with the more precise legal rule would appear to maximize coordination and predictability, Hayek observes that this appearance of predictability is illusory.¹¹⁸ In comparison to the precise terms of a particular rule, the more abstract underlying principle will both be more stable and provide a better guide to expectations about how others will behave. Whereas particular rules can change rapidly, principles change only gradually.¹¹⁹ Hayek writes:

It seems to me that judicial decisions may in fact be more predictable if the judge is also bound by generally held views of what is just, even when they are not supported by the letter of the law, than when he is restricted to deriving his decisions only from those among accepted beliefs which have found expression in the written law.¹²⁰

Moreover, articulated verbiage in written judicial opinions is only the imperfect reflection of the principles that underlie any given opinion.¹²¹ Thus it is the principle that should govern, not the precise language of the case.

The more flexible understanding of precedent from the traditional common law is captured in Hayek's characterization of the common law as a

115. See POSTEMA, *supra* note 103, at 210–17; see also Berman & Reid, *supra* note 103, at 514 (characterizing *stare decisis* as “essentially a positivist theory, more congenial to the codification movement but grafted onto the doctrine of precedent”); Caleb Nelson, *Stare Decisis and Demonstrably Erroneous Precedents*, 87 VA. L. REV. 1, 38 (2001) (noting the influence of Bentham on the American move toward stricter *stare decisis*).

116. See HAYEK, *supra* note 10, at 117.

117. See *id.*

118. See *id.*

119. This insight is elaborated in greater detail by Bruno Leoni in BRUNO LEONI, *FREEDOM AND THE LAW* (1961).

120. HAYEK, *supra* note 10, at 116. Moreover, he argues that where judicial decisions have most departed from public expectations is when the “judge felt that he had to stick to the letter of the written law” rather than informing the written law with generally accepted expectations. *Id.* at 117.

121. *Id.* at 78.

spontaneous order.¹²² Hayek does not simply characterize the virtues of a precedent-based legal system in the cost–benefit terms advanced by modern commentators, who champion stare decisis because they say it increases predictability while minimizing administrative costs.¹²³ Instead, Hayek shares the traditional view that cases are merely illustrations of more abstract legal principles; cases are not “law” in and of themselves.¹²⁴ The independent efforts of many judges deciding many cases over time generates legal principles, and it is those principles that matter, not the constituent cases themselves.¹²⁵ The legal principles that emerge from this implicit collaboration among many judges reflect greater wisdom and consensus than any individual judge deciding any individual case.¹²⁶ Thus, it is that Hayek characterizes the common law as a spontaneous order in the same way that the market is a spontaneous order.¹²⁷ Just as a market price for a particular good or service emerges from the decentralized interaction of many individuals, legal principles similarly emerge from the decentralized process of the common law.¹²⁸ Moreover, Hayek argues that the law that emerges from this decentralized common-law process will be better than legislative law or its equivalent, law imposed by a judge in a single case and followed under stare decisis in subsequent cases.¹²⁹ This is because the rule that emerges will have been tried out in several different factual contexts and found to be reasonable and in accordance with the parties’ expectations.¹³⁰ As such, the legal principle comes to be understood and relied upon in the community.¹³¹ Indeed, Hayek provocatively argues that judges do a disservice when they adhere to the letter of a precedent when it conflicts with a more coherent principle, in that it is the principle that does and should guide individual expectations, not the letter of the particular precedent.¹³²

Hayek’s view of precedent and the role of judges follows from his view of the dispersion of knowledge in society. Judges are not asked to make the “best” ruling in any given case because they are to be “passive,” as suggested by Posner, but rather because they can do better over time by deferring to

122. *See id.* at 118–22.

123. *See* POSNER, *supra* note 2, at 555 (stating that judges follow precedent, in part, because the legal certainty it promotes lowers the volume of litigation, lessens the need to hire more judges, and dilutes the power of existing judges).

124. *See* HAYEK, *supra* note 10, at 118–19.

125. *See id.*

126. *See id.* at 120.

127. *See id.*

128. *See id.*

129. *See* HAYEK, *supra* note 10, at 116–17.

130. *See id.* at 98.

131. *See* Pritchard & Zywicki, *supra* note 114, at 520.

132. HAYEK, *supra* note 74, at 26.

the accumulated knowledge of wisdom and tradition in the law. There is thus a high degree of “redundancy” in the Hayekian view of the common law that is absent from Posner’s model.¹³³ In Posner’s model, the law is only as good as a particular judge is wise. Hayek’s model, by contrast, is built on the insights of sound Burkean tradition, in that the common law reflects the accumulated knowledge of many judges collaborating over time. Indeed, Posner’s model surrenders the very purpose of Hayek’s framework—the idea that the common law is imbued with tacit knowledge that should be followed even if all of this knowledge cannot be fully understood and articulated. Thus, deference is shown to precedent not just because it reinforces individual expectations but also because the accumulation of precedent over time reflects a body of traditional knowledge that can provide a source of wisdom deeper than the learning or experience of any single or group of contemporary judges.¹³⁴ Further, this body of traditional knowledge has not been consciously designed by judges over the years. That would merely be conscious judicial planning spread out over time. Rather, it is the repeated efforts of judges to coordinate legal rules with other legal and non-legal rules that coalesce over time into a spontaneous order, allowing for interpersonal coordination.¹³⁵

B. LEVEL OF SELECTION OF LEGAL RULES

Hayek also differs from Posner in his characterization of the proper level of selection for the study of legal rules. Posner argues that there will be selection of the most efficient rules at the level of individual legal rules.

133. See Robert Sugden, *Spontaneous Order*, in 3 NEW PALGRAVE DICTIONARY OF ECONOMICS AND THE LAW 485, 488 (Peter Newman ed., 1998) (noting “redundancy” is a “crucial” property of spontaneous order).

134. See Andrew P. Morriss, *Hayek & Cowboys: Customary Law in the American West*, 1 N.Y.U. J.L. & LIBERTY 35, 40 (2005) (“Hayek assumes that judges cannot know enough to do what Posner expects them to do.”).

135. This understanding of tradition as not the accumulated wisdom of judges’ explicit views on legal problems but as the result of an evolution of legal rules interacting with each other and with society at large, helps avoid the problem of “information cascades” that have been raised as a criticism of Burkean traditionalism. See generally, e.g., Adrian Vermeule, *Common-Law Constitutionalism and the Limits of Reason*, 107 COLUM. L. REV. 1482 (2007) (analyzing the mechanisms that generate precedent and tradition); Cass Sunstein, *Due Process Traditionalism* (Univ. of Chi. Law Sch. John M. Olin Law & Econ., Working Paper No. 336 & Pub. Law & Legal Theory, Working Paper No. 158, 2007), available at http://ssrn.com/abstract_id=975538 (examining cases where the Supreme Court limited substantive due process to longstanding traditional rights). Because this concern is outside of Posner’s critique of Hayek, we do not pursue it here but merely state that the problem of information cascades applies when the Condorcet Jury Theorem is compromised through individual thinkers relying on past thinkers instead of thinking for themselves. This concern need not apply in the case of a spontaneous order because the answer to a problem (i.e., rule) is indirect as it arises out of human action *but not from human design*. See Pritchard & Zywicki, *supra* note 114, at 491 (noting that similar decisions by varied courts were generally accepted as wise and reasonable).

Hayek, by contrast, views the relevant level of selection for legal rules to be the selection among *groups* of legal rules. Hayek's selection mechanism, like Posner's, is evolutionary in nature. The difference between the two, therefore, rests in the level of selection on which they see selection pressures operating.

Posner's view of rule selection is at the level of a judge choosing between alternative individual rules.¹³⁶ Precedent binds the judge's selection of these rules, but only to the extent that the judge feels it is best to adhere to that precedent.¹³⁷ What a judge should choose, and what precedent generally entices him to choose, is the most efficient rule.¹³⁸ For Posner, a classic example is *Hadley v. Baxendale*, the famous case explicating the limits on recovery in a suit for lost profits.¹³⁹ In a *Hadley*-type scenario, *A* contracts with *B* for a service that—if performed as contracted—will result in a large profit for *A*. *B* does not know what lost profits *A* might have if he breaches his contract with *A*. *B* then breaches the contract and fails to perform the service for *A*. *A* therefore fails to achieve the profits he had hoped to garner through *B*'s service. *A* then sues *B* for the profits he did not make because of *B*'s breach. The example in *Hadley* itself was *B* fixing *A*'s crankshaft so that *A* could make money at grinding corn.¹⁴⁰ The question presented is whether *A* can recover the lost profits (what he would have made from grinding corn) or merely the cost of the service *B* failed to perform (the cost of fixing the crankshaft).¹⁴¹

To Posner, a judge faced with this question will base his decision on what is the better *individual* rule.¹⁴² The judge will review the relevant case law and, if the answer is fairly straightforward, decide whether he wants to follow those precedents or whether a different rule would be better.¹⁴³ If the precedents are not straightforward, then he can simply apply the rule of his choice.¹⁴⁴ In this way, Posner agrees with Hayek that the common law, over time, “tests” rules and gives rise to rules that are more societally useful.¹⁴⁵ However, this occurs through a process in which judges repeatedly analyze

136. See POSNER, *supra* note 2, at 560–61.

137. See *id.*

138. See *id.* at 267.

139. See generally *Hadley v. Baxendale*, 9 Ex. 341, 156 Eng. Rep. 145 (1854). See the discussion in POSNER, *supra* note 2, at 127.

140. See *Hadley*, 9 Ex. at 341–43, 156 Eng. Rep. at 146.

141. See POSNER, *supra* note 2, at 127; see also *Hadley*, 9 Ex. at 354–56, 156 Eng. Rep. at 151.

142. See POSNER, *supra* note 2, at 560.

143. See *id.*

144. See *id.*

145. See *id.* (“A rule of the common law emerges when its factual premises have been so validated by repeated testing in litigation that additional expenditures on proof and argument would exceed the value of the additional knowledge produced.”).

individual rules and assess which rule in a given instance yields a better result.¹⁴⁶

Hayek, by contrast, argues that the proper level of selection is at the meta-rule level, which is to say at the level between *societies* governed by different systems of rules.¹⁴⁷ Individual judges can choose and experiment with alternative individual rules *within* an ongoing spontaneous order, such as choosing between the rules of comparative and contributory negligence. But the overall system of rules, and its impact on society, results from the unpredictable interaction and interrelationship of all these individual rules and their interaction with individual action and, thus, are not designed by anyone. The overall *system* of rules that emerges from this group-selection process, therefore, will have aspects distinct from the particular characteristics of the rules comprising it.

For example, Hayek theorizes that capitalist societies, with rules protecting private property and free enterprise, will propagate themselves—that is, last longer and spread their systems of rules to other societies—better than noncapitalist societies because capitalist societies become wealthier and have higher rates of population growth.¹⁴⁸ The interaction between a capitalist and a noncapitalist society occurs on many different levels, including obvious examples such as rules of contract law and also nonlegal rules such as work ethic and increased cooperation between strangers.¹⁴⁹

No one person or committee selects which group of rules, or which rules within those groups of rules, are adopted by a society and which are not.¹⁵⁰ An individual rule makes sense only in context with the other legal rules of the society, plus the countless cultural customs and habits that order the society. As societies “select” systems of rules, the individual rules will relate to each other in ways that an individual judge will be unable to ascertain.¹⁵¹ Selection at the meta-level will be independent of any one individual’s choice to follow a specific rule.¹⁵² The selection will occur

146. The *Hadley* scenario is also an example of what was discussed above in Part II, namely, a rule that a judge selects to enhance efficiency but that might not actually be more efficient. Although the *Hadley* rule has been characterized as efficient, others have disagreed on the basis of empirical observation rather than armchair economic theorizing. See generally Richard A. Epstein, *Beyond Foreseeability: Consequential Damages in the Law of Contract*, 18 J. LEGAL STUD. 105 (1989) (critiquing the *Hadley* rule of damages).

147. See HAYEK, *supra* note 10, at 50, 74, 98.

148. See F.A. HAYEK, *THE FATAL CONCEIT* 120–22 (W.W. Bartley III ed., 1988); see also Morriss, *supra* note 134, at 38; Todd J. Zywicki, “Was Hayek Right About Group Selection After All?” *Review Essay of Unto Others: The Evolution & Psychology of Unselfish Behavior*, by Elliot Sober & David Sloan Wilson, 13 REV. AUSTRIAN ECON. 81, 87–88 (2000) (book review).

149. See Zywicki, *supra* note 148, at 87 nn.5–6.

150. See HAYEK, *supra* note 10, at 99 (“The rules that will spread . . . will thus, unlike commands, create an order even among people who do not pursue a common purpose.”).

151. See *id.* at 99–100.

152. See *id.* at 99.

spontaneously, and the system that wins out will simply be the system whose rules are accepted more often than the alternatives.¹⁵³

This emphasis on the group-selection aspect of legal rules also explains why Hayek believes a judge should focus on seeking to harmonize and create internal consistency among the constituent rules of the legal system. To focus on the properties of any given rule in isolation is to miss the larger point, which is to understand both how the rules that comprise the system of legal rules mesh with one another, and, perhaps even more fundamentally, the still higher level of selection regarding which behaviors should be governed by legal rules rather than some other system of social ordering, such as market exchange or voluntary civil society associations. Spontaneous orders are abstract and complex in nature; thus, individuals today generally will not know for certain which set of rules are optimal. As a result, only through competition among various rule systems do we find out which system is actually superior. Thus, as is also the case with natural selection, selection among systems of rules is inherently backward-looking because the superior set of rules can only be determined after the fact. A forward-looking judge of Posner's liking does not make sense under this approach because the choice to adopt a new rule will necessarily lack an understanding of how the rule fits in with the countless other rules of the surrounding society. However, Hayek is not completely defeatist—experience and the social sciences can provide some insight on which rule systems will most likely win out in this process. Reason can thus be a source of useful innovations in legal and social rules, but reason is an imperfect guide to selection among particular rules. In other words, although individual reason and purposive individual action can be effective for introducing variation into a system of rules, individual reason and control are too limited to know for certain whether one actually has chosen the optimal body of rules or to choose among alternative systems of rules. It is only after history and the evolutionary process of group selection have operated that one can know for sure that the most efficient rules have been adopted.

IV. THE RULE OF LAW

The foregoing discussion about the nature and purpose of the common law also helps to explain some of the differences between Posner and Hayek regarding the nature of the rule of law. Posner argues that Hayek confuses the notion of the “rule of law” with the idea of the “rule of *good* law,” which is the law of a liberal political order.¹⁵⁴ Posner thus thinks it essential to disentangle the two, arguing that Nazi Germany and the Soviet Union were, in fact, governed by the rule of law, as their legal systems contained the

153. *See id.*

154. *See* POSNER, LAW, PRAGMATISM, AND DEMOCRACY, *supra* note 1, at 281.

formal prerequisites of law.¹⁵⁵ Posner's criticisms echo those who have launched similar criticisms of Hayek's characterization of the rule of law.¹⁵⁶ It is not clear, however, that Posner and other critics have fully understood Hayek's views on the rule of law, especially as they developed over time. Just as Posner misunderstands Hayek's conception of precedent and his argument for the superiority of tacit knowledge over judicial central planning, so too Posner misunderstands Hayek's conception of the rule of law and its relationship to a spontaneous order. It may be that Hayek, in fact, committed the error ascribed to him by Posner; however, it is necessary to first fully understand what Hayek meant by the "rule of law" and why he may have been correct to use the term in the way he did.

It is true that in his early writings Hayek implicitly adopted the formalistic understanding of the rule of law advocated by Posner.¹⁵⁷ First, to meet the standards of the rule of law, government action must be "bound by rules fixed and announced beforehand."¹⁵⁸ Second, individuals must be able to know the laws and their meaning so as to behave in accordance with them.¹⁵⁹ Third, the law must apply to all persons equally.¹⁶⁰ The term "rule of law" thus was intended to generalize Hayek's observations about the common law—that it is a "purpose-independent" system designed to enable individuals to increase the predictability of each others' behavior and, thus, to better coordinate their affairs—into an animating principle for the legal system generally.¹⁶¹ A primary purpose of the rule of law, therefore, was to subject governmental behavior to the discipline of rules, but the rule of law also rightly referred to the ability to predict the behavior of *all* actors, not merely the government. Thus, the rule of law swept in the idea of the reliable enforcement of property rights and contracts and protection from tortious and criminal behavior. Following the colloquial distinction, perhaps the best definition of the rule of law was to be found by comparing it to its antithesis, the rule of men—i.e., discretionary governance by individual decision makers. Freedom for Hayek is thus not the libertarian ideal of a minimum of coercion; rather, freedom is understood as a minimum of *arbitrary* or *discretionary* coercion by others, specifically the state.

155. *See id.*

156. *See* JOSEPH RAZ, *The Rule of Law and Its Virtue*, in *THE AUTHORITY OF LAW* 210, 226–29 (1979); CASS R. SUNSTEIN, *LEGAL REASONING AND POLITICAL CONFLICT* 188–21 (1996). *But see* Todd J. Zywicki, Book Review, 8 *CONST. POL. ECON.* 355, 355–58 (1997) (reviewing CASS R. SUNSTEIN, *LEGAL REASONING AND POLITICAL CONFLICT* (1996)).

157. This discussion of Hayek's understanding of the rule of law is drawn from Todd J. Zywicki, *The Rule of Law, Freedom, and Prosperity*, 10 *SUP. CT. ECON. REV.* 1, 3–21 (2003), which further discusses Hayek's and others' related views on the rule of law.

158. F.A. HAYEK, *THE ROAD TO SERFDOM* 72 (1944).

159. F.A. HAYEK, *THE CONSTITUTION OF LIBERTY* 208 (1960).

160. *Id.* at 209.

161. HAYEK, *supra* note 10, at 85.

In his early efforts to distinguish discretionary coercion from justifiable coercion within the rule of law, Hayek implicitly endorsed the formalistic concept of the rule of law. As noted by Ronald Hamowy, however, Hayek's early understanding of the rule of law was shown to be a necessary, but not sufficient, condition of a free society governed by the rule of law. The formalistic requirements that law be articulated in advance and applied equally does reduce the threat of improper coercion; nonetheless, Hamowy contends that it does not eliminate the problem of improper coercion because the rules themselves are still created by men.¹⁶² Thus, even if the conditions for government coercion could be clearly articulated in advance, Hamowy observes that the articulated conditions themselves may have improper distinctions or undue discretion built into them. Human actors, i.e., legislators and judges, need to still *select the rules*, and thus, the law can have personal human will embedded within it, apparently providing a stamp of approval to substantial infringements on individual freedom so long as those restrictions comport with the formalistic requirements of the rule of law.¹⁶³ This critique anticipates Posner's argument that the legal systems of Nazi Germany and the Soviet Union were characterized by the rule of law, even if they were not the rule of "good" law such as would prevail in a liberal society.¹⁶⁴

Hayek, however, clearly came to believe that the English common law uniquely embodied the rule of law. To understand why, it is necessary to refer back to Hayek's view of the common law as a spontaneous order and, in particular, to the parallels he drew between the common law and the price system in markets.¹⁶⁵ Hayek's central claim in both settings was identical—the rules that emerge from the decentralized decision making of the common law, like the prices that emerge from the decentralized decision making of markets, are not made by anyone. The prices that emerge from the spontaneous order of the market system can be contrasted with a centrally planned economy, where identifiable decision makers instruct producers how to allocate resources. Similarly, the common law can be compared to other systems of law (such as civil-law systems) where rules are made by identifiable sovereign decision makers. This parallel runs both ways—just as the common law bears a conceptual resemblance to markets, Hayek's condemnation of legal positivism flows from his recognition that—

162. Ronald Hamowy, *Hayek's Concept of Freedom: A Critique*, 1 *NEW INDIVIDUALIST REV.* 28, 30 (1961); Ronald Hamowy, *Law and the Liberal Society: F.A. Hayek's Constitution of Liberty*, 2 *J. LIBERTARIAN STUD.* 287, 291–92 (1978).

163. See Leonard Liggio, *Law and Legislation in Hayek's Legal Philosophy*, 23 *SW. U. L. REV.* 507, 521, 522 (1994) (discussing the role of legislators and judges as a distinct elite class creating law to serve factional interests).

164. See *supra* note 155 and accompanying text.

165. See *supra* Part II.B–C.

in postulating the need for a sovereign decision maker—positivists were implicitly engaging in central planning of the legal system.

Understanding this concept of the common law as a spontaneous order thus helps to explain why Hayek eventually came to define the rule of law coterminously with the common law in Volume 1 of *Law, Legislation, and Liberty* (“*LLL*”).¹⁶⁶ Hayek’s extensive discussion of the common law in that volume can be best understood as his effort to reply to the critiques launched by Hamowy and others to his earlier, more formalist statement of the rule of law. In short, it appears that Hayek implicitly recognized the force of the critique that mere formalistic restraints on governmental rulemaking were necessary, but not sufficient, to build a free society. Hayek thus argues in *LLL* that under the common law, judges and legislatures do not make the fundamental laws that govern their society.¹⁶⁷ Instead, the rules generated by the common law are the outputs of a spontaneous order; thus, it is not accurate to say that they are chosen by anyone, even judges.¹⁶⁸ Hayek believes that common-law judges merely *articulate* the preexisting norms and expectations that underlie society; they do not *create* those rules.¹⁶⁹ In this “declaratory” model of the common law, rules are emergent properties from the larger common law system in the same way that prices for individual goods are emergent properties of a market system. Although Hayek’s argument that judges only “declare” the law rather than “make” it is highly contestable, it nonetheless is the cornerstone of Hayek’s response to Hamowy’s critique and provides the key to understanding the internal logic of Hayek’s argument. If it is true, as Hayek argues, that judges and political decision makers do not consciously choose rules but rather that the rules are produced by the spontaneous order of the common law and then merely declared by judges, then it seems that Hayek has addressed Posner’s critique about the relationship between the common law and a liberal order as a *logical* matter (although he may still be subject to the critique that this is inaccurate as an *empirical* matter). For Hayek, if a person is “coerced” into paying damages for breach of contract, punished for committing burglary, or prohibited from trespassing on another’s property, this coercion does not unduly infringe on his freedom. Hayek defines “freedom” as freedom from arbitrary or discretionary coercion committed by another individual; thus, where individuals are forced to follow rules that are the emergent result of an impersonal, spontaneous-order process, it is not an undue infringement

166. The following discussion draws on Todd J. Zywicki, *Reconciling Group Selection and Methodological Individualism*, in 7 *ADVANCES IN AUSTRIAN ECONOMICS: EVOLUTIONARY PSYCHOLOGY AND ECONOMIC THEORY* 267, 273–75 (Roger Koppl ed., 2004).

167. See HAYEK, *supra* note 10, at 116.

168. See *id.* at 118.

169. See *id.* at 117 (“Here the old conviction that a rule may exist which everybody is assumed to be capable of observing, although it has never been articulated as a verbal statement, has persisted to the present day as part of the law.”).

on their freedom. Under this conception of the common law, the individual person of the judge is not providing the coercion. The judge is merely articulating rules produced by an impersonal, spontaneous-order process, not creating new rules. Where decisions are based on general rules produced by impersonal and spontaneous systems (whether prices, language, or law), it becomes a logical confusion to categorize this as coercion.

Hayek illustrates the point by drawing an analogy between the legal system and the market system. It would be erroneous to believe that a farmer is “coerced” when he sells his grain in a competitive market for a price lower than he wishes. Grain prices are established by the impersonal market process; thus, when the farmer sells at the market price, one cannot claim that anyone has “coerced” him into selling the grain at the prevailing market price.¹⁷⁰ Further, when setting the price of his grain, he is not “making” that price but recognizing the price that the market has set through an impersonal process. Hayek views common law rules as emerging in society through a process fundamentally similar to the way in which prices emerge in a market. Thus, just as a farmer is not “coerced” when he sells his grain at the prevailing market price that emerges from the decentralized voluntary interactions of millions of buyers and sellers, Hayek believes that restrictions on freedom are compatible with the rule of law when individuals are coerced by legal rules that are the emergent properties of a spontaneous-order system. Additionally, when a judge enforces a legal rule, she is not “making” that rule but is recognizing a rule that has evolved through voluntary interactions in society.

To further illustrate Hayek’s intuition, the evolution of language is also a product of a spontaneous-order process. In order to communicate in a given society, one must follow certain linguistic rules and use certain words. These rules and words emerge spontaneously from the usage patterns of millions of individuals voluntarily interacting in society. Thus, in some theoretical sense, a person is “coerced” when he is forced to use a word that everyone will recognize (such as “baby”), rather than a nonsensical or foreign word that he might prefer to use. In order to communicate effectively, an individual must acquiesce in using the word according to the expectations of others. Nonetheless, Hayek suggests that it would be illogical to see it as an infringement on your freedom to be required to use the word that others expect you to use rather than your preferred nonsense word. The rules of language are the emergent product of many decentralized voluntary interactions and are not created and enforced by any particular individual or individuals; thus, Hayek suggests your freedom is not restricted

170. We leave aside the question as to whether it would be meaningful to use the term “coercion” in a monopoly context.

when you choose to use the term that emerges from the spontaneous-order process rather than an alternative term.

A legal example is the rule of consideration in contract formation. When a farmer contracts with a shipper to carry grain, both parties rely on the legal rule that their contract requires consideration to make it enforceable.¹⁷¹ If a shipper agrees to move a farmer's grain in a week's time without asking for anything in return—perhaps out of a bond of friendship—but then fails to show up and ship the grain, the farmer cannot sue for breach of contract. If the farmer brought suit, the judge would rule that no contract existed. The judge would rule this way not because she wished to set an efficient rule between the parties or to establish a future precedent, but because that is the rule that has evolved in the common law system and that the farmer and the shipper knew to rely upon. Just as not using the word “car” hinders successful communication, by not following the rule requiring consideration, the farmer will put himself at risk.

Thus, when impersonal processes generate the rules that govern social interactions, such as market prices, language, customs, or legal rules, Hayek argues that being forced to follow those rules does not improperly restrain individual freedom.¹⁷² Spontaneously created common law rules that are merely articulated by judges and not “created” by them are consistent with the requirements of the rule of law. It is the spontaneously evolved *rules* that coerce behavior, not those who discover and articulate those rules. And because the rules themselves evolve from an impersonal cultural group-selection process, Hayek argues that articulating and enforcing them is consistent with the rule of law and freedom.

It may seem that this emphasis in *LLL* on the common law is inconsistent with Hayek's original formalistic understanding of the rule of law. Unlike his later articulation of the intrinsic relationship between the common law and the rule of law, his earlier analysis emphasized the idea of the *Rechtsstaat* and the discipline of the rule of law as primarily a constraint on legislative rule-making.¹⁷³ Hayek, however, seems to have viewed his later endorsement of the common law as elaborating on, not rejecting, his earlier model of the rule of law by explaining how legal rules can emerge

171. See RESTATEMENT (SECOND) OF CONTRACTS § 71 (1979) (describing “the requirement of consideration”).

172. We note the caveat that—unlike in some legal examples—prices, language, and customs in no way “coerce” people to use them. Law, such as with criminal law, does involve coercion but, according to Hayek, only because it enforces rules of just conduct that are generally developed spontaneously. See HAYEK, *supra* note 74, at 28–29. Further, because of the nature in which it arises, the law is not an improper restraint on freedom.

173. See HAYEK, *supra* note 159, at 193–204; see also Posner, *Hayek, Law, and Cognition*, *supra* note 1, at 153. “[I]n the early part of the nineteenth century, the theoretical conception of the state of law, the *Rechtsstaat*, was systematically developed and became, together with the ideal of constitutionalism, the main goal of the new liberal movement.” HAYEK, *supra* note 159, at 199.

independently from the will of individual lawmakers.¹⁷⁴ Thus, there is no inconsistency in stating that common law rules are the result of human action but not of human design, in a way that is logically impossible under legislative rulemaking or a positivist vision of judicial decision making.

Hayek would thus likely reject Posner's purported distinction between the rule of "law" on one hand and the rule of "good law" or "liberal law" on the other. It would be equally senseless to try to draw a distinction between the "price" for a good and the "good price" for a product. The rules that emerge from the common law process, like the prices that emerge from the market process, do not fit into these sorts of conceptual categories. The congruence between a particular legal rule and the rule of law is defined in the process of its emergence, i.e., a rule satisfies the rule of law only if it is the product of an impersonal, spontaneous-order process rather than being authored by a particular individual, and it is this process by which the rule is created that defines the end of the rule of law as consistent with the rule of law.¹⁷⁵ Like true "law," a "price" is that which emerges from the impersonal, spontaneous order of voluntary exchanges in the market, not that which may be established by a rent-control board or price cap. In the case of both law and prices, the opposite of a law or a price is the command of some individual decision maker, a rule of "men." Although it is true that a particular salesclerk attaches a price tag to apples in a supermarket, it would be inaccurate to suggest that the salesclerk is thereby "making" or "creating" the price of apples, as opposed to simply articulating the prevailing market price as it emerges spontaneously through millions of individual trades. It is similarly misleading, Hayek argues, to think of a particular judge "making" law when she seeks to articulate the underlying legal principles that support a given decision. Hayek writes:

While the process of articulation of pre-existing rules will . . . often lead to alterations in the body of such rules, this will have little effect on the belief that those formulating the rules do no more, and have no power to do more, than to find and express already existing rules, a task in which fallible humans will often go wrong, but in the performance of which they have no free choice. The task will be regarded as one of discovering something which exists, not as one of creating something new, even though the result of such

174. See HAYEK, *supra* note 10, at 118–22.

175. Cf. James M. Buchanan, *Order Defined in the Process of Its Emergence*, LITERATURE LIBERTY, Winter 1982, at 5, available at <http://www.econlib.org/library/Essays/LitLbrty/bryRF1.html>. Buchanan makes a similar argument about the emergence of order in the market process: "[T]he 'order' of the market emerges *only* from the *process* of voluntary exchange among the participating individuals. The 'order' is, itself, defined as the outcome of the *process* that generates it." *Id.*

efforts may be the creation of something that has not existed before.¹⁷⁶

To be governed by the rule of law, therefore, is in fact to be governed by rules that emerge spontaneously, a process best embodied, as Hayek sees it, by the common law.

This suggests a further extension of Hayek's views of the relationship between the rule of law and a liberal social and economic order and reveals why Hayek rejects the notion that Nazi Germany was a society governed by the rule of law, which is of course a central thesis of *The Road to Serfdom*.¹⁷⁷ Hayek suggests that the "rule of law" is a concept that is meaningful *only* in a liberal society.¹⁷⁸ Indeed, given the common misunderstanding of the meaning of the term "rule of law," it may be more useful to simply refer to the type of society that Hayek has in mind as a "rule-of-law society," in the same way that we refer to an economy organized according to private exchange as a "market economy."¹⁷⁹ A rule-of-law society is indeed the society described in Part II of this Article, one in which law is a purpose-independent mechanism that enables individuals to pursue their own several ends, rather than forcing individuals to pursue ends favored by authoritative decision makers. Just as we distinguish between a market economy and a centrally planned economy, we can distinguish between a rule-of-law society and a society organized to accomplish distinct end-state social goals. A society organized by abstract and impersonal law, as opposed to the particular decisions of particular men, is in fact a liberal society. A society organized according to the commands of authoritative decision makers is something else: a society where the rule of law is meaningless.

Although what Hayek has in mind here can be difficult to tease out, it appears that he has something in mind like Michael Oakeshott's understanding of the rule of law as characterizing a civil association, as opposed to an enterprise association.¹⁸⁰ The rule of law, Oakeshott suggests, is appropriate only for a liberal social order and, indeed, serves as the central organizing and defining principle for such a society.¹⁸¹ A social order organized around end-independent rules, he observes, will produce

176. HAYEK, *supra* note 10, at 78.

177. HAYEK, *supra* note 158.

178. *See id.* at 72–79.

179. *See* WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 1383 (Philip Babcock Gove ed., 1993).

180. *See* Michael Oakeshott, *The Rule of Law*, in *ON HISTORY: AND OTHER ESSAYS* 119, 121–25, 148 (1983); *see also* Nigel Ashford, *Michael Oakeshott and the Conservative Disposition*, *INTERCOLLEGIATE REV.*, Spring 1990, at 39, 41–44 (discussing Oakeshott's theories on enterprise and civil associations); Guri Ademi, Comment, *Legal Intimations: Michael Oakeshott and the Rule of Law*, 1993 *WIS. L. REV.* 839, 865–96 (discussing Oakeshott's philosophy of the rule of law).

181. Oakeshott, *supra* note 180, at 139.

freedom, “[b]ut this ‘freedom’ does not follow as a *consequence* of this mode of association; it is *inherent* in its character.”¹⁸² He continues, “And this is the case also with other common suggestions: that the virtue of this mode of association is its consequential ‘peace’ (Hobbes) or ‘order.’ A certain kind of ‘peace’ and ‘order’ may, perhaps, be said to characterize this mode of association, but *not as consequences*.”¹⁸³

Posner, unlike Hayek and Oakeshott, rejects the argument that the concept of the rule of law is an inherently classical-liberal notion. As Oakeshott suggests, Posner is in the camp that argues that freedom and prosperity are the consequences of *following* the rule of law.¹⁸⁴ Oakeshott, and seemingly Hayek, reject this consequentialist interpretation of the rule of law as engrafting a purpose onto a purpose-independent social order.¹⁸⁵ As noted, Hayek would reject the notion that the legal system should strive for any collective goal independent of the disparate purposes of the individuals governed under that economic order. Hayek seemingly would find it similarly flawed to argue that the purpose of the rule of law is to create economic growth. Instead, the rule of law should be seen as an inherent part of a liberal social order, in that the rule of law is meaningless in a society that rejects the notion that the order exists for some purpose other than to enable the individuals who comprise it to coordinate their affairs and to interact harmoniously.¹⁸⁶ This question of social purpose brings to the fore one further aspect of Hayek’s view of the rule of law briefly discussed above: namely, that laws be generally applicable to all in society. This generality principle was a cornerstone of Hayek’s earlier work on the rule of law and is still present in *LLL*.¹⁸⁷ Hayek states that if a legal rule applies differently to different actors, then the rule is made to further a specific end above other ends.¹⁸⁸ For example, a rule that only graduates of accredited beautician schools may style hair affects graduates of those schools differently from nongraduates. It expresses a purpose—the protection against nongraduates styling hair—and a hierarchy of ends—

182. *Id.* at 161 (emphasis added).

183. *Id.* (emphasis added).

184. *Id.*; see also Zywicki, *supra* note 157, at 6–8 (explaining how the rule of law enhances individual freedom and economic prosperity).

185. Oakeshott, *supra* note 180, at 148–49.

186. *Cf.* Mack, *supra* note 15, at 263. Mack argues that Hayek does find a purpose, a telos, for law but that the purpose is not for any specific social outcome (e.g., that all children be educated). *Id.* Instead, the purpose of law is for the emergence and preservation of a social order, the specifics and the legal rules of which cannot be known ahead of time. *Id.* at 264. In other words, according to Mack, although the rules are purpose-independent with respect to the individual members of a society, the legal system is purposive with respect to the society as a whole, the purpose being the maintenance of the spontaneous order of society and the coordination and order it produces.

187. See HAYEK, *supra* note 10, at 112–15.

188. *Id.*

graduates of certain schools over nongraduates of those schools. For Hayek, such a rule is alien to a liberal social order because the law should not favor different hierarchies of ends within an order, but should merely allow an order to emerge.¹⁸⁹ Posner's view of law, on the other hand, would allow for such a rule if it furthered economic growth because the raising of economic growth over other ends is a permissible objective to the Posnerian judge or legislature.¹⁹⁰ This neutrality among actors in the articulation of law is a cornerstone of Hayek's attempt to divorce law from specific economic and social goals.

V. HAYEK, KELSEN, AND POSNER ON POSITIVISM AND LEGAL CHANGE

Finally, this explains Posner's conclusion that Kelsen "would not have subscribed to Hayek's view of 'true' (that is, good) law because he was not a Hayekian libertarian—not because he was a legal positivist."¹⁹¹ Hayek, Posner argues, could not have known a great deal about Kelsen, or indeed about legal positivism, to have said what he said about him.¹⁹² Unlike Hayek, Posner notes, Kelsen's analysis of law is "content-neutral," whereas "Hayek is interested only in content."¹⁹³ Posner concludes that Hayek simply missed the distinction.¹⁹⁴

But the foregoing may explain why Hayek did not miss the distinction. Hayek conflates what Posner calls "content" or substantive law into the rule of law itself. Law can be made in only two ways—either by designated authors (positivism) or through spontaneous-order processes. As noted, Hayek believed that traditional common-law judges did not "make" law, but rather "discovered" it.¹⁹⁵ This is the lynchpin of his argument that the law is a spontaneous order—that when a judge decided a case he simply articulated the inchoate principles embedded in the law and did not affirmatively make law.

Hayek rejected positivism because it argued that law was and should be consciously "made" and, in fact, is made by judges, legislators, or other authoritative lawmakers. As Posner notes, Hayek argued that the basic flaw of positivism was the belief that law could be devoid of any discussion of content.¹⁹⁶ Indeed, Hayek argues that with respect to private law and "especially . . . the common law," it is "simply false" to say that these laws

189. *See id.* at 119.

190. *See id.* at 23–28.

191. POSNER, LAW, PRAGMATISM, AND DEMOCRACY, *supra* note 1, at 289.

192. *See id.* at 289 (critiquing Hayek's interpretation of Kelsen's pure theory of law).

193. *Id.*

194. *See id.* at 289 (describing Kelsen and Hayek as "ships passing in the night").

195. *See supra* Part III.A.

196. HAYEK, *supra* note 74, at 44–56.

have been made by positivist lawmakers rather than emerging from a spontaneous-order process.¹⁹⁷

Posner, following the legal-realist tradition, may respond that Hayek's distinction is unrealistic—that judges in fact “make” law and that law is not “discovered” in the manner Hayek claims. Hayek, of course, responds that eighteenth-century common-law judges were not the positivist legal rule makers that they are today. Judges, he argues, did in fact believe themselves to be “finding” law, not making it, and in fact did so, and the law went awry when judges abandoned this restrained vision of their task.¹⁹⁸ Hayek argued that the law itself emerged from the decentralized spontaneous order previously described. Posner might respond that this distinction is nonsense in that it remains the case that the law is composed of the aggregation of individual judges' decisions or that the principles that underlie the law are inherently indeterminate, mandating positivist choices by judges, and thus, it remains that judges “make” the common law. But once again, this response fails to appreciate the nature of a spontaneous-order process as conceived by Hayek. If the common law is truly a spontaneous order, then it is no more accurate to say that individual judges “make” the law than it would be to say that a particular farmer “sets” the price for grain in a market when he sells at a price that finds a willing buyer or that a speaker “makes” a word when he communicates in a way so as to be understood by others. Whether law, prices, or speech, what matters is the overall order, which no one constructs.

Under the institutional structure of the traditional common law, it was difficult for judges to make new law and impose it on unwilling individuals. This was because individuals could exit a particular legal system and choose judges that would provide them with law and justice that was grounded in the expectations of the parties to the dispute rather than in serving as a means for the achievement of larger social goals. During the formation of the common law, in the several centuries before its maturity in the eighteenth and nineteenth centuries, the common law—that is, the courts of the King's Bench—was only one of many legal systems in England.¹⁹⁹ Others, public as well as private, included the courts of Chancery, ecclesiastical courts, and law merchant courts, to name only a few.²⁰⁰ Through legal fictions concerning jurisdictional rules, parties could choose which court system to submit to.²⁰¹ Judges were often paid from their courts' user fees

197. *Id.* at 46.

198. See Pritchard & Zywicki, *supra* note 114, at 460; Todd J. Zywicki, *A Unanimity-Reinforcing Model of Efficiency in the Common Law: An Institutional Comparison of Common Law and Legislative Solutions to Large-Number Externality Problems*, 46 CASE W. RES. L. REV. 961, 989–92 (1996).

199. Zywicki, *supra* note 9, at 1582–83.

200. *Id.* at 1583.

201. *Id.* at 1584.

and, therefore, had incentives to render impartial justice.²⁰² In addition, rent seekers who repeatedly played to the same judges for an expected outcome based on a particular judge's ideology did not capture those judges as easily.²⁰³ This plurality of judicial paths allowed litigants to compete between legal systems and between judges for the rulings they most preferred. Note that these were not the rulings most preferred by *plaintiffs*. This was because litigants—unlike a modern interest group, such as today's plaintiffs' bar, or a repeat player, such as a labor organization—often could not predict whether they would be a plaintiff or defendant in the next case to come along.²⁰⁴ Therefore, parties would be predisposed to seek the most predictable ruling, not the ruling that provided a precedent for increased rents in future litigation.

Law thus tended to reinforce the goals of private ordering and meeting the needs of the parties to the dispute. Judges had little opportunity or power to impose their preferred policy goals on litigants. Given this lack of power, it appears that judges did, in fact, act in the manner suggested by Hayek—they sought to discern the legitimate expectations of the parties in the disputes that arose before them. Judges simply were unable to engage in the social engineering advocated by Posner to advance efficiency, redistribution, or any other goals. Had they sought to do so, they would have lost business to rival courts that were more diligent about responding to the needs of the parties in the case at hand, rather than viewing the case as a means to accomplish larger social goals. Under this set of constraints, it is realistic to assume that judges successfully sought to “discover” the law in existing expectations, rather than “make” law.

Recent judicial innovations, such as the rise of stare decisis and appellate courts of last resort, have in many ways dramatically altered the world that Hayek is describing. Historically, again, the common law emerged from competition among many different judges acting in many different court systems with overlapping jurisdictions.²⁰⁵ Thus, judges had little power to bind other judges by authority but could do so only on the basis of the persuasiveness of their rulings.²⁰⁶ It also may be accurate to state that a supreme court today can “make” law in the way that the decentralized court

202. *Id.* at 1583. Compare this system to the use of impartial arbitrators today where each side vetoes the use of arbitrators whom each fears would be biased.

203. *Id.* at 1582.

204. Zywicki, *supra* note 9, at 1609 (“[M]ost of the disputes in question arose from conflicts between two individuals, not between institutional repeat players. Under these conditions, reciprocity norms would tend to govern the evolution of legal doctrine, rather than rent-seeking norms.”).

205. *See id.* at 1582–83.

206. *Id.* at 1577 (“It was the sound reasoning of the prior case that demanded respect, not the mere existence of the case.”).

systems of the history of the common law could not.²⁰⁷ Precedent, as noted, was a more flexible concept, such that one judge could not bind subsequent judges temporally.²⁰⁸ Subsequent judges reserved the right to reject the precedent if it was thought wrongly decided. Stare decisis, by contrast, enables a first judge in time to bind subsequent judges, thereby perhaps making it accurate to say that the first judge “makes” law to be applied by subsequent judges. These various innovations—the development of monopolistic and hierarchical court systems and the rise of stare decisis—are relatively recent in Anglo American law.²⁰⁹ Moreover, these developments dramatically increased the potential for courts to “make” law, as opposed to “finding” law, as they did in the traditional common-law world.

It is thus conventional for modern day sophisticates to reject the idea that traditional common-law judges “found” or “discovered” law, rather than “making” it. Of course, common-law judges “made” law, it is argued. For instance, Justice Scalia has written that he knows that judges “make” law but that they nonetheless should be viewed as “discovering” law because such a view limits their discretion.²¹⁰ The proper making of law, he argues, should be left to the legislature, as that embodies the democratic choice of the people.²¹¹ This view makes sense if one assumes that law must be made consciously. From this standpoint, those judges who denied that they were making law were either dishonest, in that they *knew* they were making law and just would not admit it, or naïve, in that they failed to recognize that making law was precisely what they were doing. A full understanding of the institutional constraints that historically were imposed on common-law judges suggests that it is both plausible and likely that those judges, in fact, tended to discover, rather than make, law. It is thus the anachronism of modern commentators imposing modernist, positivist presumptions on centuries-old history that may be the error in this situation.²¹²

207. See Pritchard & Zywicki, *supra* note 114, at 465; see also LEONI, *supra* note 119, at 24.

208. See discussion *supra* Part III.A.

209. Zywicki, *supra* note 9, at 1617 (explaining that these ideas did not take hold until well into the nineteenth century).

210. See, e.g., *James B. Beam Distilling Co. v. Georgia*, 501 U.S. 529, 549 (1991) (Scalia, J., concurring). In *James B. Beam*, Justice Scalia reveals that, at bottom, he is a positivist and definitely does not accept a Hayekian view of the common law:

I am not so naïve (nor do I think our forbearers were) as to be unaware that judges in a real sense “make” law. But they make it *as judges make it*, which is to say *as though* they were “finding” it—discerning what the law *is*, rather than decreeing what it is today *changed to*, or what it will *tomorrow* be.

Id.

211. Pritchard & Zywicki, *supra* note 114, at 419–20.

212. See, e.g., Richard A. Posner, *Blackstone and Bentham*, 19 J.L. & ECON. 569, 571–72 (1976) (suggesting that Blackstone was more modern and less naïve about the nature of law and the

Therefore, in faulting Hayek for criticizing Kelsen's view of the rule of law, Posner's critique rests on an apparent misunderstanding of Hayek's view of judging. If judges simply stick to judging as the historical common-law judges did, then judges will not have to try to "make" law as Posner contends they must. Allowing judges (as well as legislatures) to make law brings all the problems previously discussed, such as imperfect knowledge, disturbance of settled expectations, and incongruence among legal and nonlegal rules. Keeping judges to their traditional role allows for the spontaneous order to develop legal rules arising from the actions of the subjects of those rules and for judges to merely apply the rules to the subjects.

This brings us to one final critique of Posner's analysis of Hayek's view of law as a spontaneous order. Posner suggests that if Hayek has his way, law would stagnate under the weight of custom and not accommodate new circumstances.²¹³ Posner does credit Hayek for recognizing the utility of turning to custom in some situations, but he argues that using custom to completely define the law will create a moribund legal order:

Sometimes it makes sense for law to follow custom because custom may indeed impound the information relevant to the activity that the custom concerns. The set of customs known as the "law merchant" provided, and rightly so, the foundation of modern Anglo-American contract law. But often it makes no sense to base law on custom because a custom may reflect conditions that have changed—lacking central direction, custom tends to lag behind social and economic change—or may be the product of incentives that diverge from the socially desirable . . . Customs may in short be vestigial and dysfunctional. And again, on the crucial question of *when* law should reject custom, Hayek casts no light.²¹⁴

In the last sentence, Posner makes a very good point. Hayek did not explicate exactly when courts or legislatures should shed the hand of how legal rules were previously enforced in favor of new rules. Hayek did state that judges and legislatures should adjust legal rules over time, but perhaps, because his main concern in *LLL* was to defend law as a spontaneous order in contrast to positivism, he did not fully describe how law adjusts to change in society over time.²¹⁵

Given the earlier discussion concerning the relationship among legal rules and between legal rules and nonlegal rules, however, it is, in fact, not difficult to discern how law changes in a Hayekian legal system. In short, law

role of judges than traditionally thought); see also Albert W. Alschuler, *Rediscovering Blackstone*, 145 U. PA. L. REV. 1, 36–43 (1996) (same).

213. Posner, *Hayek, Law, and Cognition*, *supra* note 1, at 147, 152.

214. *Id.* at 162.

215. *See id.* at 149–50.

changes just as such things as technology, mores, and prices do. Law is not a fixed parameter but a variable that is changing. However, it is changing more slowly than everything else in the economy and society.²¹⁶ As actors spontaneously change the manner in which they behave, whether through technological change, cultural shifts, or other causes, law will have to change too and will change through a spontaneous-order process. Law will be the last thing to change because it, in effect, has to wait for the leaves to settle as to what order emerges from the change. When judges enforce these new legal rules, they will look to the new settled expectations, as well as previous legal rules that still shape the overall order.²¹⁷

To put some flesh on the bones of this process, we now turn to an example of how new legal rules can arise out of a spontaneous order. As several scholars have recognized, such a process of spontaneously generated new legal rules occurred among cattle ranchers in the western plains during the post-Civil War land rush.²¹⁸ After the federal government had largely cleared the land of its Native American inhabitants, prospective ranchers who reached western lands found no scarcity of opportunity.²¹⁹ These “new” lands were largely bereft of a central government or allocations of property claims, so settlers could find a vacant pasture and appropriate the land to their own use. In places such as Wyoming and eastern Montana, land was so plentiful that a rancher could be secure in his use of a valley, for example, because if another rancher came across the valley, he merely needed to move to another close by.²²⁰

This paradise did not last for long, understandably, as ranchers soon began filling up range land. With land becoming more scarce, the ranchers were faced with the question of how to determine ownership. The answer generally was that ownership went to the person who was first in possession, and claims to such possession were communicated through various means, including posted signs and newspaper notices.²²¹ Enforcement of these claims often was achieved through ranchers banding together into cattlemen’s associations.²²² For example, the Eastern Montana Stockgrowers’ Association was formed to help ranchers keep a stable system of property

216. We are indebted to Peter Boettke for this characterization.

217. Of course, a just criticism of this view asks: what will the judges look to? Will they simply poll the society to find out what actors’ new settled expectations are? Since law is a lagging indicator, that perhaps will not be necessary, though there will be some period in which expectations are not yet settled and judges will be called upon to enunciate what the law is. These are problems that we do not seek to answer here but leave for future exploration.

218. See, e.g., Terry L. Anderson & Peter J. Hill, *Cowboys and Contracts*, 31 J. LEGAL STUD. S489, S502–14 (2002); Morriss, *supra* note 134, at 42–47.

219. See Anderson & Hill, *supra* note 218, at S498–99.

220. See *id.* at S499–500.

221. *Id.* at S500.

222. *Id.* (discussing first-possession claims and how it was in the mutual interest of cattlemen to enforce these claims through cattlemen’s associations).

rights over their various cattle domains.²²³ Under this system, a rancher's claim would be staked out by the area his cattle had been using.²²⁴ However, because of the vast terrain and lack of materials, fences were not practical, and a rancher's cattle would invariably wander into neighboring pastures.²²⁵ The rancher would then call upon the help of other Association members in the area to help him collect his herd, often through a biannual roundup during which all neighbors were expected to help out.²²⁶ The same would later be expected of him to assist other Association members.²²⁷ If a rancher refused to assist in this manner, his fellow ranchers would later withhold assistance from him.²²⁸

Out of these associations grew the recognition of where ranchers' property rights lay.²²⁹ This included the extent of a rancher's real estate as well as the extent of his obligations to other ranchers and their obligations to him.²³⁰ All of this arose through a spontaneous process of actors adapting to new circumstances by applying old expectations (such as loyalty and noncommunal ownership of land) and forming new, but settled, expectations (such as assisting in a roundup).²³¹ If a Hayekian judge were to encounter such a situation, the proper references would be all of these things: the old expectations, the new circumstances, and the new, but settled, expectations. The judge would decide not by creating a new rule that he believed to be optimal for the situation, but rather by recognizing the rules of the society and enforcing them as they best fit with each other. The legal rules would necessarily lag behind the economy, technology, and morals because they would arise out of them.

This example does not fully answer Posner's critique of Hayek and custom, but it illustrates how changes in custom lead to changes in law and, therefore, how increased efficiency in society can lead to increased efficiency in law. Expectations change just as society changes, and law will change along with them. How a judge will discern when a new legal rule has arisen is a question that Hayek left to another day, and a question that Posner rightly stated deserves an answer.²³² However, the answer to that question is surely less vexing than how a judge (a human being limited in knowledge) can craft new legal rules out of whole cloth in an attempt to introduce added efficiency, or some other goal, into society. Hayek might conclude that the

223. *See id.* at S500–01.

224. Anderson & Hill, *supra* note 218, at S500.

225. *Id.* at S502.

226. *Id.*

227. *Id.*

228. *See id.* at S503.

229. *See* Anderson & Hill, *supra* note 218, at S500–01.

230. *See id.*

231. *See id.*

232. *See* Posner, *Hayek, Law, and Cognition*, *supra* note 1, at 150.

former question may be hard to answer but that the latter is impossible. The latter involves a judge, or a legislature, trying to find out what has changed and how a new legal rule should be crafted so as to respond to that change. The former merely involves discovering what the settled expectations are in the new order. The crafting is largely left to the spontaneous-order process.

VI. CONCLUSION

Posner's critique of Hayek is fundamentally based in a belief that judges should purposely shape the law toward greater efficiency. Further, Posner sees Hayek's view that judges should merely reinforce expectations as one that would leave the law static, moribund, and unable to adapt to an ever-changing society. Also, Posner views Hayek's understanding of the rule of law as confused, and he believes that Hayek inappropriately substituted "law" with "the rule of law." As we have seen, this critique rests on three fundamental distinctions between his views and Hayek's.

First, Posner believes that individual rules of law can be viewed separately from the larger legal and societal order. On the contrary, Hayek argues that an individual rule is as it is because it has grown out of the system of expectations embodied within a larger set of rules, and that set includes not only legal rules, but also nonlegal rules of customs and morals. When courts enforce community expectations, they should look not just to the most recent case on point—the strict doctrine of *stare decisis*—but to the concepts that underpin the relevant case law and the larger order the case law exists within. Thus, enforcing the expectations of the community will not result in a static and formulaic reinforcement of norms propounded by fallible human actors, i.e., judges, but the application of the rules of a spontaneously formed societal order that necessarily *does* respond to the changing needs of society, as that order reflects the rules that society's members continually create by their actions but not by their design.

Second, and very closely related to the first distinction, Posner holds that judges can know what legal rules will lead to socially desirable results. In contrast, Hayek argues that such forward-thinking "law making" is merely another form of central planning destined to fail in some degree because of the limits of human knowledge. Posner's reaction to this argument is that this is true in the case of a centrally planned economy but not necessarily so on the level of a judge forming an individual rule.²³³ There, an individual

233. *See id.* at 164. Posner argues that Hayek, and the Austrian School of economics as a whole, have not "offered convincing reasons for believing that instrumental reasoning guided by economic models can never improve government regulation . . ." *Id.* Posner suggests that customs may become "vestigial and dysfunctional" and that Hayek offers no answer as to when lawmakers should—as Hayek admits occasionally must happen—reject custom. *Id.* at 162.

truly can access the information available and “legislate” a better rule.²³⁴ This again, however, circles back to the first assumption—that a rule can be examined independently of its larger legal and societal order. To “make” law with proper knowledge, a judge must know how these rules interrelate with the individual rule in question and what the consequences will be to the other rules with the change to the individual rule. This, again, argues Hayek, is knowledge that no one expert judge, or group of judges, can know.

Third, these distinctions lead Posner to misunderstand Hayek’s conception of the rule of law. For Hayek, the rule of law is not simply the nonarbitrary enforcement of preexisting rules. It is also the enforcement of rules that have been formed through a spontaneous process. Kelsen and Posner, on the other hand, as positivists, view law as arising through conscious decision making. Under a positivist conception of law, the rule of law describes any legal system where laws, however created, are duly made and obeyed. However, under Hayek’s conception such a process is not a complete description of the rule of law. Although consciously designed rules may be called “law,” they do not make for a “rule of law,” as they are the outcome of human design. In other words, “man made” law is an example of the rule of men. For Hayek, only in a liberal order, with a process such as the common law to allow a spontaneous order of law to arise, can the rule of law reign. Further, only in a liberal order can law properly change in tandem with the changes that arise in that order.

234. *But see* Donald J. Boudreaux, *Hayek’s Relevance: A Comment on Richard A. Posner’s Hayek*, *Law & Cognition*, 2 N.Y.U. J.L. & LIBERTY 157, 163–65 (2006) (arguing that Posner places too much faith in the power of planners who necessarily lack complete information).